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No.

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1980

GRANT-BILLINGSLEY WHOLESALE LIQUOR CO., INC.,
Appellant,

v.

MICHAEL C. LENNEN, SECRETARY OF REVENUE
FOR THE STATE OF KANSAS, et al.,
Appellees.

On Appeal From the Supreme Court of the State of Kansas

JURISDICTIONAL STATEMENT

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QUESTIONS PRESENTED

The alcoholic beverage industry in Kansas operates on three independent vertical tiers, including producers, wholesalers and retailers, all of whom are licensed, private enterprises. Kansas is a "license" state, as compared with those "monopoly" states in which the state itself conducts all or part of the business.

For many years, Kansas had "open" wholesaling, under which, subject to credit considerations, producers were obliged to sell to all wholesalers. Under a recent statute ("H.B. 2020"), Kansas requires distilleries and wineries to enter into written territorial agreements with wholesalers, with each producer required to contract with and to sell to only one wholesaler in each territory. H.B. 2020 further forbids wholesalers from selling outside their exclusive territories.

H.B. 2020 totally bans intrabrand competition, regardless of market circumstances or competitive effects. H.B. 2020 originated in a proposal sponsored by a wholesaler trade association. It shields wholesalers from any competition in the brands they carry, regardless of wholesaler market power or of the market share of the brands they represent. The statute puts no limits on the number of brands or the number or size of territories a wholesaler may tie up in the state. H.B. 2020 also severely curtails the ability of producers to replace incumbent wholesalers or to alter the scope of exclusive territories. H.B. 2020 sets up *no* state supervision of the iron-clad territorial restraints that it mandates.

A state trial court struck down the wholesaler fiefdom aspect of H.B. 2020 on federal antitrust grounds. The

Kansas Supreme Court upheld the statute and reversed the trial court. In an opinion rendered shortly before this Court's *Midcal* decision of last Term, the highest state court ruled that the Twenty-first Amendment absolutely overrode the Sherman Act and that H.B. 2020 was not repugnant to the antitrust laws of the United States. The Kansas court explicitly rejected the line of California decisions subsequently approved by this Court in the *Midcal* case. When this Court announced *Midcal,* appellant immediately urged this Court's decision upon the Kansas Supreme Court in connection with a motion for rehearing. The rehearing request was considered, but was denied without opinion.

The questions presented are:

1. Whether the Kansas Supreme Court may disregard *Midcal* by ruling that the Twenty-first Amendment wholly immunizes anticompetitive state liquor statutes.

2. Whether a state liquor statute that prevents intrabrand competition by prohibiting a wholesaler from selling outside its allocated territory, curtails the replacement of incumbent wholesalers, and declares exclusive territorial allocations *per se* legal, in each instance, regardless of market circumstances and wholly without state supervision, is invalid under federal antitrust law.

3. Whether a state statute that resulted in (i) an end to all intrabrand competition in relevant markets with high producer concentration and extensive product differentia-

tion, (ii) a severe wholesaler oligopoly, dominated by two statewide wholesalers, and (iii) horizontal territorial arrangements between remaining wholesalers is invalid under federal antitrust law.[1]

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[1]*List of all parties in the Court below.* The following were parties, directly or by intervention, to the proceedings in the court whose judgment is sought to be reviewed: Grant-Billingsley Wholesale Liquor Co., Inc.; Kansas Distributors, Inc.; Colby Distributing Co., Inc. (which left the business and withdrew from the case); Michael C. Lennen, Secretary of Revenue, State of Kansas; Thomas J. Kennedy, Director of Alcoholic Beverage Control, Division of the Department of Revenue, State of Kansas; Albert P. Campbell, Michael P. Sarras, and Richard D. Martens, all members of the Kansas Alcoholic Beverage Control Board of Review; the State of Kansas, ex rel. Vern Miller, District Attorney for the Eighteenth Judicial District; Standard Liquor Corporation; and the Kansas Retail Liquor Dealers Association. A trial court order of August 3, 1979, granted *amici* status to A-B Sales, Inc., Lux-Witmer Company, Inc., d/b/a Sunflower Sales Company of Topeka, and Eastern Distributing Co., Inc.

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JURISDICTIONAL STATEMENT

Grant-Billingsley Wholesale Liquor Co., Inc., the appellant, appeals from the final judgment of the Kansas Supreme Court holding that the Twenty-first Amendment wholly negates the Commerce Clause and the Sherman Act and holding that H.B. 2020, which amends certain provisions of the Kansas Liquor Control Act, K.R.S. 41-101, *et seq.*, on its face and as applied is not repugnant to the Sherman Act and the Supremacy Clause of the Constitution of the United States.

OPINIONS BELOW

The opinion of the Kansas Supreme Court, reprinted as Appendix A hereto,[2] is reported *sub nom. Colby Distribu-*

[2]The appendices to this jurisdictional statement are occasionally cited hereinafter as "App."

ting Co., Inc. v. Lennen, at 606 P.2d 102 (1980). The opinion of the state trial court, the District Court of Shawnee County, Kansas, is not reported and is reprinted as Appendix B, *infra.* The case proceeded by direct appeal from the state trial court to the highest state court; accordingly, there is no intermediate state appellate court opinion.

JURISDICTION

Appellant brought this case to secure a declaratory judgment of the invalidity of H.B. 2020 under federal antitrust law and an injunction against its enforcement. The judgment of the Kansas Supreme Court upholding H.B. 2020 was entered on January 19, 1980. Appendix A, *infra.* That court considered appellant's motion for rehearing but denied it without opinion on April 9, 1980. Appendix C, *infra.* Appellant filed notices of appeal in the Kansas Supreme Court and in the state trial court (to which the record has been returned) on June 25, 1980. Appendix D, *infra.* Mr. Justice White, as Circuit Justice, extended the time for filing this jurisdictional statement to and including August 6, 1980. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(2).

CONSTITUTIONAL AND STATUTORY PROVISIONS

This case involves the following constitutional and statutory provisions, in pertinent part:

U.S. Const., Art. I, § 8, cl. 3 (Commerce Clause):

> The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States. . . .

U.S. Const., Art. VI, cl. 2 (Supremacy Clause):

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be

bound thereby, any thing in the Constitution or Laws of any State to the contrary notwithstanding.

U.S. Const., Amendment XXI, § 2:

> The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited.

Section 1 of the Sherman Act, 15 U.S.C. § 1:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal.

Section 2 of the Sherman Act, 15 U.S.C. § 2:

> Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony. . . .

H.B. 2020 (Kansas "Territorial Franchise System"):

> Due to its length, the pertinent text of H.B. 2020 is set out in Appendix E, *infra.*

RAISING THE FEDERAL QUESTIONS

In its pleadings, briefs and arguments in the state trial court, appellant drew in question the validity of H.B. 2020 on the grounds of its repugnancy to federal antitrust law and the Supremacy Clause. That court struck down the provisions of H.B. 2020 now at issue on the federal grounds that appellant asserts in this Court.

The federal law questions were again briefed and argued on the direct appeal to the Kansas Supreme Court, and that court also ruled on them directly, reversing the trial court and upholding the state statute. Appellant put the line of California decisions subsequently approved by this Court in *California Retail Liquor Dealers Association v.*

Midcal Aluminum, Inc., No. 79-97, OT 79 (100 S.Ct. 937, March 3, 1980) before the Kansas courts at all pertinent stages. When *Midcal* came down from this Court, it was put before the Kansas Supreme Court in conjunction with appellant's motion for rehearing.

STATEMENT OF THE CASE

This case concerns the validity under federal antitrust law of the wholesaler territorial exclusivity arrangements that H.B. 2020 recently brought about in Kansas. H.B. 2020 significantly changed the wholesale liquor business in the state.

A. Open Wholesaling Before H.B. 2020

Distilled spirits and wines are sold in Kansas under a three-tier distribution system. Distillers and vintners sell to wholesalers (distributors), who in turn sell to retailers. No person licensed at one level of this system may have an interest in a licensee operating at another level (known as the "tied-house" prohibition, K.R.S. 41-312). The state itself does not do business at any level of the industry. The requirement of three tiers is unaffected by H.B. 2020 and is not at issue in this case.

Before H.B. 2020, Kansas required "open" wholesaling. All brands of spirits and wine sold in the state were carried by all distributors, without defined "territories" or "franchises." K.R.S. 41-1011. A state regulatory agency set minimum prices to retailers and consumers. *Id.*, § 41-1115.

In the years immediately before H.B. 2020, nine distributors did business in the state, serving approximately 1,200 retailers. C.T. 12.[3] The largest of these distributors

[3] "C.T." references are to the clerk's transcript of the trial court record. "R.T." references are to the reporter's transcript of the trial conducted before the state trial court. "R.T.(I)" refers to the first volume of the transcript, and "R.T.(II)" to the second.

had about 25% of the total wholesale business in 1978, the second largest about 20%, with the remaining seven distributors having fragmented, smaller shares. *Id.*, 13-14. These market shares were changed dramatically by H.B. 2020.

B. H.B. 2020: Airtight Territorial Restraints and the Total Elimination of Intrabrand Competition

1. THE TOTAL ELIMINATION OF INTRABRAND COMPETITION

H.B. 2020, reprinted in Appendix E, *infra*, became law in May, 1979. The statute effects a complete swing from "open" wholesaling (all brands for all wholesalers) to total elimination of intrabrand competition by requiring exclusive, airtight territorial agreements between individual producers and wholesalers.

H.B. 2020 requires producers and Kansas distributors to make written agreements allocating impenetrable territorial monopolies to particular distributors for particular brands. A distributor may sell only to retailers within its territory (although that territory may be the entire state). H.B. 2020 permits no intrabrand competition, since a producer may enter into an agreement with only one distributor for each brand in each territory (dual distributors are prohibited), and a retailer may buy only from the exclusive distributor appointed by the producer for the retailer's area. There is no limit upon the number of producers or brands that one distributor may tie up in the state; accordingly, interbrand competition may be reduced to a "shadow-boxing" exercise within the sales force of a single distributor. *See, e.g.*, R.T.(II), at 66. Indeed, the statute apparently would sanction a single-firm, wholesale monopoly.

2. THE ABSENCE OF STATE SUPERVISION

Although H.B. 2020 provides that written territorial agreements between producers and distributors must be

filed with a state regulatory agency, there is no state supervision of the restraints created by these private agreements. Neither H.B. 2020 nor any other statute sets out guidelines regarding the size or number of intrabrand monopoly territorial allocations which may be granted to any one wholesaler, the number or market dominance of the brands allocated to a particular wholesaler, the permissible market shares of wholesalers, the duration of the restraints, or any other core antitrust interest. There is no regulatory mechanism for supervision or re-examination—active, continuing, pointed or otherwise—of the airtight territorial allocations or their intensely anticompetitive effects.

3. ENTRENCHMENT OF WHOLESALER MARKET POWER

H.B. 2020 sets no time limits on the mandated restraints. Moreover, the statute provides that once a territorial agreement is reached, it may not be modified, altered or terminated except for "reasonable cause." App. E, at 49a-50a. The "reasonable cause" impediment to termination or modification of the restraints is not defined. Nonetheless, the incumbent, entrenched distributors are authorized to go to court to enforce the "reasonable cause" provision against any producer that attempts to alter its distribution arrangements. State regulatory agencies are given no role in this matter. Thus, a producer that wishes to increase the efficiency of distribution patterns or to terminate an incompetent wholesaler confronts the substantial deterrent of costly litigation under a hopelessly vague legal standard, unclarified by regulation. Since producers cannot designate duplicate distributors and as a practical matter cannot switch distributors, they cannot prevent disfavored treatment of their brands.

H.B. 2020 also shields the incumbent wholesalers from competition by blocking new entry. Because of H.B. 2020,

the incumbents have sewn up wholesale distribution of the brands sold in the state. A potential new entrant at the distributor level is unlikely ever to be able to obtain brands to distribute in the state. This also means that new producers desiring to sell in the state who cannot interest the incumbents in new brands may not be able to obtain distribution.

C. How H.B. 2020 Went Into Effect

H.B. 2020 went into effect in two stages, each originally designed to be of two months' duration. C.T. 38-42. During phase I (May 10 to July 10, 1979), wholesalers and producers were directed to enter into the contracts that would set up the mandated territorial exclusivity. *Id.*, 38-39. This was an "open season" for tying up brands, and there was a scramble for exclusivity wholly unregulated by the state. Phase I was supposed to end on July 10, 1979, but a trial court order kept it open temporarily, with the result that phases I and II came to a close roughly simultaneously. App. A, at 6a; C.T. 43-44.

Phase II (July 11, 1979 to September 10, 1979) was designed to be a transitional period during which wholesalers who lost out in phase I would dispose of their inventories in brands they could no longer represent. C.T. 39-41. On September 10, 1979, H.B. 2020 went into full effect. App. A, at 12a.

The state alcoholic beverage regulatory agency in Kansas categorizes spirits into separate classifications (rum, vodka, gin, varieties of whiskey, etc.) and keeps official records of the annual volume of sales of each category in the state.[4] Industry publications and the dis-

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[4]These official state market share documents and data were introduced into evidence by the defendant state officials at trial. See Kansas Division of Alcoholic Beverage Control "Report Concerning

tributors themselves adopt the same classifications. R.T. (I), at 12; R.T. (II), at 58-59; C.T. 34-35. The combination of the contracts formed during phase I (the "sign-up" period) plus the official records made it possible to know with precision by mid-July, 1979, when this case was initiated, the market shares of spirits producers selling in the state and the post-H.B. 2020 market shares held by the wholesalers who obtained contracts during the phase I implementation period. See R.T.(I), at 11-23; plaintiffs' trial exs. 2-5; defendants' trial ex. 1.

The state market share data demonstrate that in each category of spirits, a handful of distilleries has the bulk of the business. The data, coupled with trial testimony, show that H.B. 2020 was superimposed on relevant markets dominated by a small number of producers, dealing in heavily advertised, strongly differentiated products—scarcely an environment conducive to wide-open interbrand competition, or likely to be improved by the introduction of absolute intrabrand restraints.

The state data show that in the instance of rum, for example, one producer has 90% of the business. In blended whiskies, as another example, one producer has 63.4% of the business, with a two-firm concentration ratio of 86.8%. Light whiskies evidence comparable duopoly characteristics. In fact, most of the categories of spirits sold in the state exhibit a high concentration ratio at the producer level.[5] Moreover, spirits brands and categories are strongly

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Shipments of Alcoholic Liquors by Classification and Brands from Distillers to Kansas Distributors for Fiscal Year July 1978 through June 1979." R.T.(I), at 16-20; defendants' trial ex. 1.

[5]The one, two, three and four firm concentration ratios for the categories of spirits sold in the state are set forth in Appendix F, *infra*.

differentiated in consumer perception. R.T.(I), at 45-46; R.T.(II), at 67-69.

H.B. 2020 eliminated intrabrand competition in the highly concentrated categories of spirits sold in the state. It also further diminished the already limited interbrand competition, for it created severe oligopoly at the distributor level. Two distributors, Standard and Famous, obtained statewide franchises for many of the dominant spirits brands. Plaintiffs' trial exs. 2-5; defendants' trial ex. 1. Standard ended up with almost 50% of the wholesale spirits business in the state and Famous with about 25%. *Ibid.*

The remaining distributors formed two groups. Each group allocated areas among its members and then, as a unit, sought contracts from the producers. R.T.(I), at 23; R.T. (II), at 29-31, 42. The first group is referred to as "Combo III." The second group, which included appellant, Kansas Distributors, Inc., and Colby Distributing Co., has been all but shut out of the market. Apellant's share of the spirits market has fallen from 7.63% to about two and one-half percent. C.T. 14; R.T. (I), at 25. The share for Kansas Distributors, Inc., has been reduced from 9.74% to slightly more than three percent. C.T. 14; R.T.(II), at 27. Colby sold its assets to Standard, the now dominant wholesaler, and to Combo III.

Yet another distributor, D. A. Winters Co., also left the business. The realistic sum of these developments is that H.B. 2020 reduced participation in the wholesale spirits business in the state from nine separate firms to three, the third "firm" being a horizontal combination.

The following data, taken from plaintiffs' trial ex. 2, illustrate by volume of case purchases the degree of dominance H.B. 2020 conferred on the two largest spirits wholesalers:

Category	% Standard	% Famous	% Together
Rum	95.09	2.28	97.37
Tequila	88.06	6.79	94.85
Blended Whiskey	64.58	29.24	93.82
Brandy	70.50	16.85	87.35
Cocktails	69.30	15.17	84.47
Canadian	59.91	22.04	81.95
Scotch	36.45	42.80	79.25
Flavored Vodka	72.57	—	72.57
Gin	28.24	43.97	72.21
Vodka	34.01	18.10	52.11

D. The Trial Court Proceedings and Ruling

1. TRIAL COURT PROCEEDINGS

Appellant and two other wholesalers brought this action in state court in July 1979, against the pertinent state officials, seeking an injunction against implementation and enforcement of H.B. 2020 and a declaration of its invalidity under Sections 1 and 2 of the Sherman Act, as well as other grounds. On July 17, 1979, a state trial judge temporarily enjoined phase I of H.B. 2020 and set the matter for expedited trial on the merits. C.T. 43-44. Thereafter, a county district attorney, the Kansas Retail Liquor Dealers Association, and wholesalers other than the plaintiffs came into the case, either as intervenors or *amici*, for and against the validity of H.B. 2020. App. B, at 24a; C.T. 85. The matter was tried in state trial court on August 6 and 7, 1979.

At trial, both sides presented evidence as to the effects of H.B. 2020 upon competition at both the producer and distributor levels. In addition to documentary market share data, including the materials mentioned above, there was considerable testimony as to the economic effects of H.B. 2020.

Dr. William T. Terrell, an economist, testified against H.B. 2020. For a period of time before the enactment of H.B. 2020, Dr. Terrell undertook an independent study of liquor distribution in Kansas. R.T.(I), at 112.[6] Terrell testified that H.B. 2020 would shift the wholesale market away from competition and towards monopoly, *id.*, 115, and that the statute threatened grievous and pernicious anti-competitive effects. *Id.*, 116. He testified that under the former law, the existence of rivals for sales of particular products to retailers led to lower prices, good delivery service and adequate inventories of products. *Id.*, 119-20. Distributors could not raise prices above state minima for particular brands, for other distributors carrying the same brands would simply take the business. *Id.*, 120. H.B. 2020 would substantially eliminate this pro-competitive effect. *Id.*, 123-25.

Dr. Terrell further explained that H.B. 2020 insulates distributors from competition from new entrants, since it fails to provide the means for new entry by wholesalers, by tying the available brands exclusively to the surviving incumbents. R.T.(I), at 123-24. Terrell pointed out that H.B. 2020 inevitably would eliminate some of the existing distributors for reasons unrelated to the free play of competitive forces. *Id.*, 124-25. Under H.B. 2020, prices to consumers will increase to reflect the monopoly status of the surviving wholesalers. *Id.*, 129. Terrell characterized the probable effect of H.B. 2020 as the exclusion of all but the most powerful wholesalers, leading ultimately to monopoly profits for the survivors. *Id.*, 137. H.B. 2020, Dr. Terrell concluded, serves no one's interest except the powerful surviving distributors. *Id.*, 130.

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[6]Terrell's study was referred to by the Kansas Supreme Court as an "excellent discussion of the historical and economic background of alcoholic liquor in Kansas. . . ." App. A, at 4a-5a.

Defendants called State Senator Frank Gaines to testify as to the legislative history of H.B. 2020. R.T.(I), at 59. Gaines testified that he headed an interim committee, the Special Committee on Liquor Laws, which heard testimony from various interested parties before submitting proposed legislation which became H.B. 2020. *Ibid.* As the court below noted, "H.B. 2020 was the result of the Committee's study." App. A, at 5a. Frederick M. Switzer, counsel for the Wine and Spirits Wholesalers of America (WSWA), appeared before the Committee and was particularly influential in its deliberations. R.T.(I), at 66. Gaines testified that Switzer's work on alcoholic beverage distribution systems was presented to the Committee, *id.*, 69, and that Senate Bill 28, which as amended became H.B. 2020, was written by Mr. Switzer in St. Louis, the headquarters of WSWA. *Id.*, 82. WSWA is a trade association representing the interests of member wholesalers.

Senator Gaines acknowledged that some distributors would "go under" as soon as H.B. 2020 was "determined." R.T.(I), at 86. He also testified as to the total lack of state supervision of the H.B. 2020 distributor territories. He admitted that the matter was left entirely to the discretion of the private parties involved, R.T.(I), at 85, and further conceded that there were no state guidelines regarding the allocation of the exclusive territories. *Id.*, 98.

Jack F. Grant, president of appellant, testified that his company lost two-thirds of its sales following the enactment of H.B. 2020, R.T.(I), at 25, and that that kind of decline would eventually put Grant-Billingsley out of business. *Id.*, 26. Mr. Grant also described the pernicious effect of H.B. 2020 upon interbrand competition. He pointed out that there had been interbrand competition before H.B. 2020, *id.*, 45, but that afterwards leading brands would be controlled by the same wholesaler. *Id.*, 51-52.

This detrimental effect upon interbrand competition was also brought out in testimony by Leslie J. Rudd, President of Standard Liquor Corporation, the Kansas distributor made dominant by H.B. 2020. Mr. Rudd conceded that under the prior law, competition between distributors kept prices down to the lowest level permitted by law. R.T.(II), at 61-62. He also agreed that under H.B. 2020, Standard, as an exclusive distributor, would be free to set prices at levels it chose. *Id.,* 60. As to interbrand competition, he further agreed that the only competition generated between brands in the same category which his company distributed would be within his own company's sales force. *Id.,* 66.

2. TRIAL COURT RULING

On August 31, 1979, the state trial court issued a memorandum opinion and judgment on the validity of H.B. 2020. App. B. Following findings as to the anticompetitive nature of H.B. 2020, the trial court concluded, *inter alia,* that:

(a) the Twenty-first Amendment does not *pro tanto* repeal the Commerce Clause, from which the Sherman Act derives, but merely requires that each constitutional provision be considered in the light of the other (App. B, at 34a);

(b) H.B. 2020 compelled private parties to engage in anticompetitive territorial agreements without state supervision and in violation of the Sherman Act (*id.,* 36a); and

(c) H.B. 2020's monopoly franchise regime bore "no reasonable rational relation to the purpose of fostering temperance and orderly marketing conditions" and "does not tend to preserve public health, safety or welfare but has a tendency to stifle legitimate business by creating a monopoly or trade barrier, in violation of the Sherman Act. . . ." *Ibid.*

The trial court invalidated the territorial exclusivity provisions of H.B. 2020. The court temporarily held up its judgment, to permit the state defendants to take an immediate direct appeal to the Kansas Supreme Court.

E. The Kansas Supreme Court Decision

The Kansas Supreme Court initially stayed the judgment of the state trial court, permitting H.B. 2020 to go into full force and effect on September 10, 1979, the originally scheduled date for full effectiveness. On the merits, the highest state court upheld H.B. 2020, reversing the trial court on both Twenty-first Amendment and federal antitrust grounds.

1. THE TWENTY-FIRST AMENDMENT RULING

The highest state court first ruled that the Twenty-first Amendment gave the state absolute control over the liquor industry, wholly unrestricted by the Commerce Clause or by federal antitrust law. App. A, at 15a-18a. The court entered this ruling while the *Midcal* case was *sub judice* at this Court. The Kansas court cited the California line of decisions culminating in *Midcal* (subsequently affirmed by this Court), but concluded that the California decisions were "contrary to our law and without precedent in Kansas." *Id.*, 20a. Although presented with the opportunity on rehearing to correct its ruling to reflect this Court's *Midcal* decision, the Kansas Supreme Court declined to do so, without opinion. App. C.

2. THE RULINGS ON FEDERAL ANTITRUST LAW

In addition to its Twenty-first Amendment ruling, the court below found "another rationale for upholding H.B. 2020." App. A, at 18a. That "rationale" was the court's conclusion that H.B. 2020 comported with the Sherman Act, for two reasons—neither of which, it should be noted, is supported by citation to any Sherman Act authorities.

First, the court saw no difficulty in the fact that because of H.B. 2020, two wholesalers ended up with the exclusive right to distribute two-thirds of the spirits brands sold in the state.[7] This was because H.B. 2020 had left all wholesalers in the state free to attempt to corner the market during the phase I sign-up period, and the fact that the bidding for market dominance had gone to the strongest not only did not offend the Sherman Act but was what barefisted competition was all about. In the court's words, H.B. 2020 presented:

> ". . . ample opportunity for each [wholesaler] to exercise its own perseverance to obtain products and territory. If one or more fails to obtain its share of the market the law is not at fault; it is one of the hazards of a free market." App. A, at 19a.

Second, the court stated that H.B. 2020 allowed "sufficient brand and price competition to withstand allegations of a violation of the Sherman Anti-Trust Act." *Ibid.* This was because "there are now at least two distributors operating in every area of the state . . . ," *id.*, 19a, and each "distributes different brands, which compete with one another." *Ibid.* In placing its reliance on interbrand competition, the court failed to note that previously there had been nine wholesalers carrying all competing brands and that because of H.B. 2020, one wholesaler ended up with as much as ninety-five percent of a particular category of

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[7]The Kansas court attributed market shares of about 30% to each of the dominant wholesalers. App. A, at 18a. The court misunderstood the evidence offered on this point. It is true that Standard and Famous each represent about 30% of the spirits brands sold in the state. R.T.(I), at 22. However, these two wholesalers obtained the popular, dominant brands which sell in larger volume than other brands. *E.g.*, R.T. (I), at 16, 48-49. Accordingly, on a volume of sales basis—the actual market share—Standard and Famous obtained about three-fourths of the business. Plaintiffs' trial exs. 2-5; defendants' trial ex. 1.

spirits throughout the state and very large shares of other categories. Apparently the court's theory was that so long as all brands were not allocated to the dominant wholesaler, there was sufficient interbrand competition to uphold a total ban on intrabrand competition.

Nor did the court address the high degree of concentration at the producer level of the industry and the strong degree of product differentiation in the business, factors that bear on the unlikelihood of healthy interbrand competition in Kansas, regardless of the structure of the wholesale level of the industry. The court was equally silent on why it should be presumed that interbrand competition would be vigorous at the wholesale level under the severe oligopolistic conditions brought about by H.B. 2020.

3. STATE ACTION

The court below conceded that the "size of the franchise territory and the designation of brands are left to private agreement. . . ." In short, there was no state supervision. However, in the opinion of the court, this was a plus rather than a negative for the validity of H.B. 2020, for leaving such market restraints to private agreement was "under the best traditions of a free society." App. A, at 20a.

4. THE STATE INTERESTS UNDERLYING H.B. 2020

H.B. 2020 contains no statement of state purpose. In various passages of its opinion, the Kansas Supreme Court listed a number of state interests thought to be advanced by H.B. 2020. The court referred to promotion of temperance and orderly markets, protection of the general welfare, health and safety of the people of Kansas, increasing state tax revenues and curbing illegal importation by reducing retail prices and thus reducing the tendency of consumers to buy out of state, and passing of the results of competition on to consumers. App. A, at 5a, 7a-8a, 20a, 22a-23a.

The court did not articulate how lower retail prices, assuming that H.B. 2020 brought them about, would promote temperance, orderly marketing conditions, or the general welfare, health and safety of the people of Kansas. Nor did it indicate how the bestowal of intrabrand monopoly power on the surviving wholesalers would advance those interests. Nor did the court deal with the conflict between two of the purposes it attributed to H.B. 2020—hold up retail prices to promote temperance and protect retailers from price competition, yet reduce retail prices to discourage consumers from buying out of state.

The interests of curbing illegal out-of-state buying by Kansans and thereby increasing state tax revenues through increased sales in Kansas depend, as the court recognized, App. A, at 8a, 20a, on the achievement of lower retail prices. Yet the court did not discuss whether extensive price competition was likely in a substantial oligopoly, where intrabrand competition is forbidden.[8]

THE QUESTIONS ARE SUBSTANTIAL

A. Midcal Requires Reversal of the Kansas Court's Twenty-first Amendment Ruling

The court below ruled that the Twenty-first Amendment permits Kansas to enact liquor legislation wholly unfettered by the Commerce Clause and, therefore, by the Sherman Act. The last full paragraph of the state court's opinion, App. A, at 22a-23a, suggests that this reading of the Twenty-first Amendment colors every aspect of the court's decision. As shown by the *Midcal* decision of last Term,[9]

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[8] *See* "Law hasn't cut Kansas liquor cost," *Kansas City Star*, p. A-1 (July 8, 1980) (state records show that retail prices have risen since H.B. 2020).

[9] *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, No. 79-97, OT 79, 100 S.Ct. 937 (1980).

the lower court's interpretation of the Twenty-first Amendment is plainly erroneous. Because the Kansas court has already denied rehearing in the face of *Midcal*, the appropriate disposition of this case would appear to be summary reversal. The antitrust aspects of the case suggest the same disposition.

B. H.B. 2020 Is Invalid on its Face under Federal Antitrust Law

In H.B. 2020, Kansas has attempted to repeal the Sherman Act with respect to territorial restraints. The state has ordered wholesale substitution of the unencumbered and unsupervised self interest of private parties for the competitive processes and concerns protected by the Sherman Act. The significance of such an attempt is obvious. If Kansas lawfully can do what it has attempted here, the Sherman Act and the other federal antitrust laws will have no effect in those states with private liquor lobbies strong enough to persuade the state legislatures that competition is not in the public interest.

H.B. 2020 is so evidently invalid on its face under federal antitrust law that further inquiry is unnecessary, further proceedings below would be pointless, and summary reversal is the correct disposition. This conclusion follows from the facial implications of H.B. 2020 and the basic requirements of federal antitrust law, wholly apart from the facts of what happened in Kansas as H.B. 2020 went into force and regardless of the appropriate Sherman Act standard (*per se*, rule of reason, or other category) to apply to the statute.

H.B. 2020 requires that all wholesalers enter into agreements which absolutely prohibit their right to sell outside of a designated territory. The restrictions on termination or modification of territories in the statute augment the exemption from competition extended to wholesalers. H.B. 2020 creates "[t]erritorial monopolies, intrabrand. . . ."

In re Coca-Cola Company, 91 F.T.C. 517, 612 n.12 (1978). These "airtight" territorial restraints[10] are required regardless of the market share of the affected producer, the market share of the distributor, or any other relevant facts. Furthermore, H.B. 2020 contains no provisions which allow the state to evaluate or approve the mandatory territorial restraints agreed to by private parties, and the state has no power to modify the territories established by their agreements. H.B. 2020 thus attempts to create an absolute bar to any consideration of the market effects of privately established agreements, contrary to this Court's decisions requiring economic analysis for the purpose of determining whether a non-price vertical restraint amounts to an unlawful, unreasonable restraint of trade.

As noted below, H.B. 2020 should be subjected to a standard of *per se* illegality or, at a minimum, presumptive invalidity, because of the intensely anticompetitive nature of the restraints it mandates. However, even if one assumes that H.B. 2020 falls under rule of reason analysis, it is nonetheless patently invalid on its face because it excludes consideration of the very economic and other factors that the rule of reason demands be taken into account. Since the statute is facially invalid under standard rule of reason analysis, it is *a fortiori* invalid under any more stringent test.

This Court's decision in *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977) substituted a rule of reason for a *per se* approach to the general run of non-price vertical restraints. However, "[t]hat a practice is not *per se* unlawful does not mean that it is *per se* lawful." *Eiberger v. Sony Corp. of America*, 1980-2 Trade Cas. ¶ 63,328, at 75,692 (2d Cir. 1980). The rule of reason under

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[10]*See Pitofsky, The* Sylvania *Case: Antitrust Analysis of Non-Price Vertical Restrictions,* 78 Colum. L. Rev. 1, 4 n.10 (1978).

the Sherman Act requires a "careful assessment" and a "discriminating examination" of economic and market factors in analyzing the legality of particular restraints of trade. *Broadcast Music, Inc. v. Columbia Broadcasting System,* 441 U.S. 1, 16, 24 (1979). H.B. 2020 forbids *any* assessment or examination, much less a careful and discriminating analysis, of the private restraints it compels. It attempts to declare all such restraints *per se* lawful in perpetuity, regardless of the circumstances. H.B. 2020 is, accordingly, invalid on its face, regardless of the appropriate Sherman Act standard which should be applied to it. As to this pure point of law, the facts of the proceedings below are irrelevant.

C. On the Record Presented, H.B. 2020 Is Invalid Under Federal Antitrust Law

This Court's *Sylvania* decision did "not foreclose the possibility that particular applications of vertical restrictions might justify *per se* prohibition. . . ." 433 U.S., at 58. The manifestly anticompetitive nature of the airtight restraints mandated by H.B. 2020 justifies application of the residuum of the *per se* rule permitted by *Sylvania. See id.,* at 49-50, 58; Pitofsky, *supra,* 78 Colum. L. Rev., at 8-9, 28-34. At a minimum, such particularly anticompetitive restraints should be subject to a "rule of presumptive illegality." Baker, *Vertical Restraints in Times of Change,* 44 Antitrust L.J. 537, 544-46 (1975); Zelek, et al., *A Rule of Reason Decision Model After* Sylvania, 68 Cal. L. Rev. 13, 29-36 (1980). *Accord,* F.M. Scherer, Industrial Market Structure and Economic Performance 510 (1970) ("hard-boiled" rule of reason).

In the face of these authorities, the court below apparently applied an eviscerated rule of reason approach—so long as a scintilla of interbrand competition could be hypothesized, the most egregious forms of perpetual intra-

brand restraints were lawful, regardless of market conditions, degree of market power, efficiency of market performance, or any other pertinent factor. The approach of the Kansas Supreme Court is erroneous even under the rule of reason. On the record presented, this Court should reverse, correct the erroneous approach followed below, and establish the governing legal standard for restraints on competition such as the ones H.B. 2020 mandates.

1. The dangers of a statute such as H.B. 2020 are not unique to Kansas. The distilled spirits industry exhibits nationally a high degree of market concentration. *E.g.*, *Impact*, September, 1979. A wealth of authority recognizes the particular importance of preserving a maximum of intrabrand competition when interbrand competition is impaired by extensive market concentration. *E.g.*, Zelek, et al., *supra*, 68 Cal. L. Rev., at 30; Pitofsky, *supra*, 78 Colum. L. Rev., at 35; Louis, *Vertical Distribution Restraints After* Sylvania, 76 Mich. L. Rev. 265, 274-77 (1977); Strasser, *Vertical Territorial Restraints After* Sylvania, 1977 Duke L.J. 775, 802; ABA Antitrust Section, Monograph No. 2, *Vertical Restrictions Limiting Intrabrand Competition* 63-64 (1977); L. Sullivan, Handbook of the Law of Antitrust § 149 at 429 (1977). *See Sylvania, supra*, 433 U.S., at 51 n.19 (validity of intrabrand restraints presumes healthy interbrand competition); 63-64 (White, J., concurring) (stressing Sylvania's "faltering, if not failing" market position). Nonetheless, liquor wholesaler statutes designed to inhibit intrabrand competition exist in a number of states. Several of these statutes approach the extreme degree of anticompetitiveness exhibited by H.B. 2020.[11] All of these statutes curb interbrand rivalry in an

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[11] *See, e.g.*, Me. Rev. Stat. tit. 28, § 665 *et seq.*; Vt. Stat. Ann. tit. 7, § 701 *et seq.* *See also* Ga. Ad. Code § 560-2-3-.10. *See* F. Switzer, The Three-Tier System of Distribution in the Wine and Spirits Industry 17 (1975), defendants' trial ex. 2.

industry where the degree of market concentration mandates maximum preservation of intrabrand competition.

Midcal means that these anticompetitive franchise statutes, enacted before *Midcal,* will now be subjected to antitrust scrutiny. The issue is of national importance, and this Court should settle the governing antitrust standards applicable to such statutes.

2. This Court declared in *Midcal* that: "The Twenty-first Amendment grants the States virtually complete control over whether to permit importation or sale of liquor and *how to structure the liquor distribution system.*" 100 S.Ct., at 946 (emphasis added). In the context of the full opinion, the emphasized language logically could not have been intended to shelter private market allocation schemes any more than private price fixing schemes. Judging by footnote 9 of *Midcal*, by the literal terms employed, and by full context, the language emphasized above addresses state ownership of some part of the business or such structural matters as the three tier requirement in Kansas, which is not challenged in this case.

Nonetheless, the *Midcal* "virtually complete control" language is being cited in defense of restrictive state statutes relating to liquor distribution, as in, for example, *Norman Williams Company v. Rice*, Court of Appeal for the Third Appellate District, State of California (July 17, 1980).[12] This Court should end any ambiguity on the

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[12]*Norman Williams* involves a California statute prohibiting a licensed importer from purchasing or accepting delivery of any brand of distilled spirits unless designated as an authorized importer of that brand by the brand owner or its agent. Applying *Midcal*, the state intermediate appellate court (the same court affirmed by this Court in *Midcal*) struck down the statute. The decision is subject to further review within California.

The state appellate court in *Norman Williams* confronted the *Midcal* language emphasized above. The state court concluded that

point, which has considerable significance to a number of state liquor statutes across the country.

3. H.B. 2020 constitutes "plain protectionism." Baker, *supra*, 44 Antitrust L.J., at 543. It is a blatant special interest statute that springs from anticompetitive purposes and that produces sharply anticompetitive effects.[13] The competitive harms are not simply to intrabrand competition but also to interbrand concerns. Statutes like H.B. 2020 directly suppress new entry at the wholesaler level and indirectly at the producer level (new producers have difficulty obtaining distribution), and they are an invitation to horizontal coordination. Their effects "approximate horizontal market allocation." Pitofsky, *supra*, 78 Colum. L. Rev., at 9. The arrangements they create deserve invalidation as a horizontal evil. *See* L. Sullivan, *supra*, at 431. *See United States v. Sealy, Inc.*, 388 U.S. 350 (1967).

Despite the severe anticompetitive harms inflicted by H.B. 2020, which appear to contravene not only Section 1 of the Sherman Act but also Section 2, the court below upheld the statute simply by hypothesizing an increase in interbrand competition. The hypothesis defies credulity

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the "how to structure the liquor distribution system" phrase of *Midcal* addressed such basic structural matters as whether to install a licensing system but did not shield the "primary source" requirement of the state statute before the court from the Commerce Clause.

[13] *Cf. National Society of Professional Engineers v. United States*, 435 U.S. 679, 692 (1978) (emphasis added, footnote omitted):

> ". . . [T]he purpose of [antitrust] analysis is to form a judgment about the competitive significance of the restraint; it is not to decide whether a policy favoring competition is in the public interest, *or in the interest of the members of an industry*. . . . [T]hat policy decision has been made by the Congress."

in the circumstances, because precisely the opposite occurred, but of greater importance, such an approach would eviscerate even the rule of reason as applied to such patently offensive statutes. This Court should clarify the error in the approach followed below and further clarify that the state interests purportedly at stake either bear no rational relationship to the requirements of H.B. 2020 or are outweighed by the severity of harm to fundamental federal antitrust interests.

If the restraints brought about by H.B. 2020 were legal, there was no need for the statute. H.B. 2020 can only be an attempt to exonerate restraints otherwise unlawful, to provide an insurance policy against the Sherman Act. However, only Congress can repeal the Sherman Act, and it has not done so for the liquor industry. Thus, the only basis for a contention that H.B. 2020 is valid is the Twenty-first Amendment. Yet *Midcal* holds that the Twenty-first Amendment does not protect unsupervised private agreements which contravene the antitrust laws.

CONCLUSION

For the foregoing reasons, the decision below should be summarily reversed or, alternatively, the appeal should be given plenary consideration.

Respectfully submitted,

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Appendix A

In the Supreme Court of the State of Kansas

No. 51428

January 19, 1980

Colby Distributing Co., Inc., et al.,
Appellees,

v

Michael Lennen, et al.,
Appellants.

Syllabus by the Court

1. Pursuant to the Twenty-first Amendment, a state may absolutely prohibit the manufacture, transportation, importation, sale or possession of alcoholic liquors irrespective of when or where produced or obtained, or the use to which they are to be put, and may adopt measures reasonably appropriate to effectuate those prohibitions and exercise full police authority in respect to them, unfettered by the due process clause, the equal protection clause or the commerce clause.

2. The constitutionality of a statute is presumed, all doubts must be resolved in favor of its validity, and before the statute may be stricken down, it must clearly appear the statute violates the constitution.

3. In determining constitutionality, it is the court's duty to uphold a statute under attack rather than defeat it and if there is any reasonable way to construe the statute as constitutionally valid, that should be done.

4. In a civil action, the record is examined and it is *held:* The trial court erred in holding pertinent sections of House Bill 2020 unconstitutional.

HERD, Justice:

This is an action seeking a declaratory judgment and permanent injunction from the enforcement of 1979 amendments to the Kansas Liquor Control Act (K.S.A. 41-101 *et seq.*). The amendments were enacted by the legislature, effective May 10, 1979 and are designated House Bill 2020. The trial court found the act constitutional but found certain sections of the amendments in violation of the Sherman Anti-Trust Act. 15 U.S.C. § 1 *et seq.* We hold H.B. 2020 constitutional, thus reversing in part and affirming in part the judgment of the trial court.

A brief discussion of the history of Kansas liquor laws will be helpful in understanding the issues before us. In 1880, Kansas amended its constitution providing for prohibition. Kan.Const. art. 15, § 10. Bootleggers and illegal saloons flourished, however, until Carry Nation and others aroused public indignation by their attacks on illegal liquor traffic at the turn of the century. Feelings of both anti-saloon and pro-saloon forces became increasingly violent until finally, urged on by the fear of armed conflict, the legislature passed laws making it a penal offense for one to give another a drink of alcoholic liquor, to be found in a place where it was sold, to sell it and finally to possess alcoholic liquor. L.1881, Ch. 128, §§ 2, 10. The latter was known as the "bone dry law."

Ultimately in 1948, the citizens of Kansas recognized prohibition neither ended liquor consumption nor eliminated its sale. The constitution was amended to permit the legal sale of liquor. L.1947. Ch. 248, § 1. As a result the Kansas Liquor Control Act (K.S.A. 41-101 *et seq.*) was passed in 1949 ending 69 years of constitutional prohibition. It provided for the regulation of the manufacture, distribution, sale, possession and consumption of alcoholic liquors. The act has remained virtually unchanged except for the 1965 Private Club Act (K.S.A. 41-2601 *et seq.*) and the 1978 Restaurant Club Act (K.S.A. 1978 Supp. 41-2601 *et seq* and K.S.A. 1978 Supp. 41-803). It provides for a three-tiered distribution system composed of a manufacturer, distributor and retailer, none of whom may own any interest in the other and all are licensed by the state.

The original law required that alcoholic liquor be sold subject to the provisions of the Kansas Fair Trade Act (G.S. 1949, 50-301—50-310) which effectively established a minimum price. The Fair Trade Act was declared unconstitutional and void, in violation of Art. 2, § 1 of the Constitution of Kansas, in 1958. *Quality Oil Co. v. du Pont & Co.*, 182 Kan. 488, 322 P.2d 731 (1958). During the 1959 legislative session, a liquor price control act was enacted which governed the sale price of alcoholic liquors. In 1961 it was found unconstitutional by this court on the grounds it was an unauthorized delegation of legislative authority to private persons without guidelines. *State, ex rel. v. Mermis*, 187 Kan. 611, 358 P.2d 936 (1961).

Immediately following that decision, the legislature enacted the liquor price control law (K.S.A. 41-1111—41-

1121) which remained effective until H.B. 2020 went into effect. It provided that the pricing began with the manufacturer who must sell to the distributor at a price "as low as the lowest price for which the item is sold anywhere in any state in the continental United States . . . ." K.S.A. 41-1112. This is known as a price affirmation law. It should be noted the legislature delegated the authority to fix the beginning price on liquor to the manufacturer from prices determined by competition. This arrangement was held valid in *Laird & Company v. Cheney,* 196 Kan. 675, 414 P.2d 18 (1966).

After the manufacturer established the beginning price and had it affirmed, the Alcoholic Beverage Control Board of Review (ABC) established a reasonable markup for the distributor and retailer taking into consideration all business costs and a reasonable profit. Each distributor was authorized to sell any brand of liquor anywhere in the state to any retailer. This system is known as "open franchising." In addition, it prohibited retailers from purchasing from a manufacturer and having him send invoices to distributors who in turn would bill the retailer with the goods sent directly from manufacturer to retailer. Kansas requires the liquor to be shipped exclusively to the distributor's warehouse. This is known as an "at rest" law. Kansas law also requires distributors to purchase liquor only from brand owners or manufacturers, or their exclusive agents. This purchase arrangement has been categorized as a "primary source" law. An excellent discussion of the historical and economic background of alcoholic liquor in Kansas is found in an unpublished article, "The

Status of Alcoholic Liquor in the State of Kansas: A Progress Report," written by William T. Terrell, Associate Professor of Economics at Wichita State University.

Reflecting constituent complaints on pricing and ABC complaints of illegal retail purchases out of state, the 1978 legislature created a Special Committee on Liquor Laws to conduct a study seeking remedies for the complaints. H.B. 2020 was the result of the Committee's study.

Briefly, H.B. 2020 is an attempt to obtain liquor prices which are competitive with surrounding states by introducing competition into the three-tiered structure. The affirmation technique at the manufacturer level was retained but at the distributor level, H.B. 2020 permits the distributor to negotiate brand franchise contracts for a territory statewide area or less, and allows the price to seek its own level in the market place as a result of competition between brands. The wholesale price established by the competition plus a reasonable markup determined by the ABC Board then becomes the retailer's minimum price to the consumer. The distributor must respect the franchise territory he has acquired and may not sell outside that area. There were nine licensed liquor distributors in Kansas at the time of trial: Standard Liquor Corporation; Grant-Billingsley Fruit Co., d/b/a Grant-Billingsley Wholesale Liquor Co., Inc.; Colby Distributing Co., Inc.; Kansas Distributors, Inc.; Eastern Distributing, Inc.; A-B Sales, Inc.; Sunflower Sales Co.; Famous Companies, Inc.; and D. A. Winters Co., a sole proprietorship. Neither Famous nor Winters are parties or intervenors in this suit. Colby sold

its business to Standard during the pendency of the appeal. The Wholesale Dealer's Association supported the passage of H.B. 2020; however, after its enactment, in the scramble for brand franchises, Colby, Grant-Billingsley, and Kansas Distributors were unsuccessful in obtaining the brands or area they sought. Standard and Famous each obtained statewide franchises on numerous popular brands of liquor. A-B Sales, Sunflower and Eastern Distributing were satisfied with their franchises, although the areas are less than statewide and are for fewer brands than Standard and Famous. The franchise alignment resulted in at least two wholesale competitors for all types of alcoholic liquor in every area of the state.

H.B. 2020 became effective May 10, 1979, but provided all distributors would have 120 days thereafter to dispose of the accumulated inventories of liquor brands for which they had not obtained a franchise. This action was filed July 17, 1979, by Kansas Distributors, Colby and Grant-Billingsley, against the secretary of revenue, director of alcoholic beverage control and members of the Alcoholic Beverage Control Board of Review. At that time, the trial court entered a temporary restraining order preventing implementation of H.B. 2020 until August 31, 1979.

On August 3, 1979, Standard, A-B Sales, Sunflower and Eastern were permitted to intervene in opposition to plaintiff's position; Vern Miller, Sedgwick County District Attorney, and The Kansas Retail Liquor Dealers Association intervened in support of the plaintiffs. It was never clarified by the parties why the district attorney of Sedgwick county was permitted to intervene on behalf of the people of Kansas in opposition to the attorney general.

The case was tried August 6 and 7, 1979. Plaintiff's evidence consisted of the testimony of John F. Grant, president of Grant-Billingsley Wholesale Liquor Co. and Albert C. Becker, president of Kansas Distributors, Inc., both of whom testified they did not oppose H.B. 2020 until they discovered they could not obtain the brand franchise or the territory they had anticipated. They stated Standard and Famous each held statewide franchises on a number of well known brands of wines and distilled spirts representing 32.33% and 31.83%, respectively of the total brands sold. They introduced documents showing the specific brands each had negotiated with suppliers. Both witnesses admitted plaintiffs had mutually agreed Colby would take the western Kansas territory, Grant-Billingsley central Kansas, and Kansas Distributors, Inc. eastern Kansas. Each would have the same brands, altogether constituting a statewide franchise. They further testified that as a result of Famous and Standard obtaining statewide franchises on so many popular brands, their projected volume would be reduced by two-thirds and they would be driven out of business.

Plaintiff's one other witness was William T. Terrell, a Wichita State University economist who had made a study of the Kansas Liquor Control Act. He testified in his opinion the exclusive franchise provisions of H.B. 2020 would create a wholesale liquor monopoly. He also stated, however, that under the law prior to H.B. 2020, Kansas was more of a control or monopoly state than a license state.

Defendants called Sen. Frank Gaines who testified the legislature intended to maintain the three-tiered liquor

control system in Kansas and passed H.B. 2020 as an exercise of the police power to lower prices to the consumer, maintain an orderly market and eliminate the importation of illegal liquor from out of state, thereby collecting more taxes within the state.

The defendants also called Leslie J. Rudd, president of Standard Liquor Corporation. He testified there would be brand competition under H.B. 2020 because of the proprietory or economic interest each distributor had in his franchised brands. That interest would create a savings in freight costs, a reduction in warehouse inventory and a more efficient operation, all resulting in a savings to the consumer. He also testified the prices he had filed with the ABC for September were below the prices for the same brands previously filed under the old law.

The challenge to the bill's constitutionality generally centers around the actions dealing with exclusive franchising and price fixing by distributors. The sections under attack are too lengthy to include in this opinion. We have therefore, included the trial court's brief summation of the pertinent sections of H.B. 2020.

> "a. Sec. 2 allows distributors to sell only such brands of alcoholic liquor to only those retailers whose licensed premises are located within the geographic territory for which such distributor is authorized to sell such brand as designated in the notice or notices filed with the Director pursuant to Sec. 3;
>
> "b. Sec. 3 prohibits any distributor from selling any alcoholic liquor in this state unless such distributor has filed with the Director a written notice stating each geographic territory as has been agreed upon be-

tween such distributor and a distiller within which such distributor shall sell to retailers one or more brands of such distiller. Said section further provides that no distiller shall grant such a franchise for the distribution of a brand to more than one distributor for all or part of any designated territory. Said section likewise proscribes and limits in subsections (3), (4), (5) and (6) the ability of any such distiller or such distributor to terminate or modify any such franchise or to alter the geographic territory designated in such franchise agreement, except for reasonable cause;

"c. Sec. 4 prohibits any distributor of alcoholic liquor from selling a brand or kind of such liquor to any retailer whose licensed premises are located outside said distributor's exclusive franchise territory for such brand as established under Sec. 3 described hereinabove. Sec. 4 further prohibits any distiller or distributor from fixing, maintaining, coercing or controlling the resale price of such alcoholic liquor to be resold by such distributor or distiller, but specifically authorizes distributors to furnish licensed retailers with a price list of the retail minimum price, including the minimum mark-up, for all such liquor sold by such distributors to such retailers;

"d. Sec. 5 prohibits any distributor of alcoholic liquor from purchasing any such liquor from any distiller unless such distiller shall file with the Director a written statement agreeing to sell any of the brands or kinds of such liquor manufactured and distributed by such distiller to any distributor licensed in this state and having a franchise to distribute such brands of such liquor, pursuant to Sec. 3, and to make such sales to all franchised distributors at the same current price and without discrimination and to file periodic price lists showing their current prices with the office

of the Director. Sec. 5 further prohibits any licensed retailer from purchasing any such liquor from any such distributor unless such distributor shall file with the Director a written statement agreeing to sell any of the brands or kinds of such liquor distributed by such distributor and to provide service in connection therewith to any licensed retailer whose licensed premises are located within the geographic territory of such distributor's franchise for such liquor, to make such sales to all such licensed retailers at the same current bottle and case price, and without discrimination and to file price lists showing such current bottle and case price in the office of the Director periodically;

"e. Sec. 6 specifically provides that the sales price of alcoholic liquor sold by distiller to licensed distributors of alcoholic liquor shall be no higher than the lowest price for which same is sold to distributors anywhere in the continental United States, and that the minimum mark-ups of such liquor to be sold by retailers licensed in this state should be determined and regulated by the ABC Board and thereby eliminates from any regulation whatsoever the price at which such liquor can be sold by distributors to retailers and the minimum price at which such liquor can be sold by retailers to consumers;

"f. Sec. 7, Sec. 8, Sec. 9 and Sec. 10 deal with the establishment of ABC Board of minimum mark-up which shall be charged by retailers in sales of alcoholic liquor to consumers;

"g. New Sec. 11 provides for a period of 120 days or until September 10, 1979, wherein a presently licensed distributor, such as the Plaintiffs herein, may sell any alcoholic liquors that such distributor may

have on hand at the time this Act takes effect in the same manner, and to the same purchasers as such distributor was authorized to sell the same prior to May 10, 1979."

Section 14 is the amending and repealing portion of the bill.

The trial court rendered its decision August 31, 1979. It found:

"4. The state has the right to establish and regulate franchise areas under the police power to regulate the liquor industry so long as these laws do not interfere or impede valid federal law or constitutional safeguards. Providing for suppliers and distributors to establish exclusive franchise areas without state intervention or state power to control or regulate has no reasonable rational relation to the purpose of fostering temperence and orderly marketing conditions. The effect of the exclusive franchise system authorizes private persons to engage in anti-competitive conduct and constitutes a violation of the Sherman Act.

"5. It is even more pernicious to allow price fixing with an exclusive franchise to sell, both controlled by the same non-government entity, without regulation by the state.

. . . . .

"Therefore, the following sections are declared void in accordance with these findings, conclusions and decisions:

a. Section 7
b. Section 8
c. Section 9
d. Section 10

"12. The following sections are valid except as follows:

a. New Section 3(1)—Delete 'No manufacturers, importer or other supplier shall grant a franchise for the distribution of a brand to more than one distributor for all or part of any designated territory.'

b. Section 6—Delete 'and (b) that minimum mark-ups on alcoholic liquor sold by retailers licensed in this state should be determined and regulated by law.'

c. Section 10(2)—Delete 'plus minimum mark-up.'

All other sections are valid."

A permanent injunction was granted with the judgment barring implementation and enforcement of the invalid portions of H.B. 2020.

On September 5, 1979, the trial court denied defendants' application for an injunction pending an appeal, which enabled the defendants and the ABC Board to continue operating under the prior law, but stayed the judgment until September 10, 1979. Defendants perfected their appeal and on September 10 requested a stay of H.B. 2020 and the trial court's judgment pending the appeal. This court stayed the trial court's order but refused to stay H.B. 2020 which became effective that day.

The plaintiffs cross appealed on September 17, 1979, placing all of the issues raised by the pleadings and the judgment of the trial court before this court, challenging the constitutionality of H.B. 2020.

For purposes of clarity, we will hereafter refer to the plaintiffs as appellees and the defendants as appellants.

We will begin our discussion by reviewing several well established rules pertaining to legislative enactments.

> "It is fundamental that our state constitution limits rather than confers powers. Where the constitutionality of a statute is involved, the question presented, is therefore, not whether the act is authorized by the constitution, but whether it is prohibited thereby. [Citations omitted.]
>
> "The constitutionality of a statute is presumed, all doubts must be resolved in favor of its validity, and before the statute may be stricken down, it must clearly appear the statute violates the constitution. [Citations omitted.]
>
> "In determining constitutionality, it is the court's duty to uphold a statute under attack rather than defeat it and if there is any reasonable way to construe the statute as constitutionally valid, that should be done. [Citations omitted.]
>
> "Statutes are not stricken down unless the infringement of the superior law is clear beyond substantial doubt. [Citations omitted.]
>
> "Courts do not strike down legislative enactments on the mere ground they fail to conform with a strictly legalistic definition or technically correct interpretation of constitutional provisions. The test is rather whether the legislation conforms with the common understanding of the masses at the time they adopted such provisions and the presumption is in favor of the natural and popular meaning in which the words were understood by the adopters. [Citations omitted.]" *State ex rel. Schneider v. Kennedy,* 225 Kan. 13, 20-21, 587 P.2d 844, 850 (1978).

City of Baxter Springs v. Bryant, 226 Kan. 383, 598 P.2d 1051 (1979).

As a result of the stays granted in this litigation, in addition to the legislative 120 day delay postponing the effective date of the act (new Section 11, H.B. 2020), the provisions of H.B. 2020 were not in effect on the date of trial, rendering the evidence presented highly speculative. Our concern here is primarily with the constitutionality of the provisions of H.B. 2020 on its face. Appellees allege sections 2, 3, 11 and 14 violate the Sherman Anti-Trust Act and, as such, are invalid under the supremacy clause of the U.S. Constitution. U.S. Const., art. VI, cl.2.

In considering any state law regulating intoxicating liquors, we must begin with the Twenty-first Amendment, the second section of which provides:

> "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

The manufacture, sale and use of intoxicating liquors has traditionally been a subject of governmental regulation at both federal and state levels. Such regulation is viewed as a valid exercise of the police power to protect the public health, welfare and morals. See *Crane v. Campbell,* 245 U.S. 304, 38 S.Ct. 98, 62 L.Ed. 304 (1917); *Mugler v. Kansas,* 123 U.S. 623, 8 S.Ct. 273, 31 L.Ed. 205 (1887); *The License Cases,* 46 U.S. 504, 12 L.Ed. 256 (1847). When the Eighteenth Amendment was repealed in 1933 by the Twenty-first Amendment, each state was granted broad regulatory power over liquor traffic within its borders.

That regulatory power included the authority to completely forbid the importation of liquor if a state so desired. *U. S. v. Frankfort Distilleries,* 324 U.S. 293, 65 S.Ct. 661, 89 L.Ed. 951 (1945); *State Board v. Young's Market Co.,* 299 U.S. 59, 57 S.Ct. 77, 81 L.Ed. 38 (1936). A state's power to regulate intrastate operations of liquor traffic is not restricted by the commerce clause. *Ziffrin, Inc. v. Reeves,* 308 U.S. 132, 60 S.Ct. 163, 84 L.Ed. 128 (1939). In *Hostetter v. Idlewild Liquor Corp.,* 377 U.S. 324, 330, 84 S.Ct. 1293, 1296. 12 L.Ed.2d 350 (1964), the Supreme Court held that "a State is totally unconfined by traditional Commerce Clause limitations when it restricts the importation of intoxicants destined for use, distribution, or consumption within its borders." That holding was more recently affirmed in *Seagram & Sons v. Hostetter,* 384 U.S. 35, 42, 86 S.Ct. 1254, 1259, 16 L.Ed.2d 336 (1966).

Although the Twenty-first Amendment grants broad regulatory powers to a state with regard to intrastate regulation of liquor traffic, a state may not exercise exclusive control over liquor shipments passing through its borders which are destined for interstate use. See *Hostetter v. Idlewild Liquor Corp.,* 377 U.S. 324, 84 S.Ct. 1293, 12 L.Ed.2d 350; and *Collins v. Yosemite Park Co.,* 304 U.S. 518, 58 S.Ct. 1009, 82 L.Ed. 1502 (1938).

It is argued the state's almost absolute regulatory control recognized in *Seagram & Sons* was modified in *Craig v. Boren,* 429 U.S. 190, 97 St.Ct. 451, 50 L.Ed.2d 397 (1976). In that case, the Supreme Court struck down an Oklahoma law which prohibited the sale of 3.2% beer to males under the age of 21 and females under the age of 18. Okla.

Stat. tit. 37, §§ 241 and 245 (1958 and Supp. 1976). The court found the "gender-based differential" contained in the statutes constituted a denial of equal protection to males between the ages of 18 and 20. Because the case concerned statutes pertaining to liquor regulation, the court discussed the role of the Twenty-first Amendment and whether the power it conferred upon states in the field of liquor regulation was strong enough to withstand an equal protection challenge. The court held "the Twenty-first Amendment does not save the invidious gender-based discrimination from invalidation as a denial of equal protection of the laws in violation of the Fourteenth Amendment." *Craig v. Boren*, 429 U.S. at 204-205, 97 S.Ct. at 461. The issues before the court did not directly involve an application of the Commerce Clause. The court did, however, reaffirm the rule that while the Twenty-first Amendment did not repeal the Commerce Clause, the Amendment "created an exception to the normal operation of the Commerce Clause." *Craig v. Boren*, 429 U.S. at 206, 97 S.Ct. at 461. That exception is clearly the overwhelming power granted the states in the area of liquor regulation. We find the issues before the court in *Craig* did not directly involve the state's regulatory power in liquor traffic and the earlier holdings conferring that power were not modified.

This court has followed the rationale of U.S. Supreme Court cases, commencing with *State v. Payne*, 183 Kan. 396, 403, 327 P.2d 1071, 1078 (1958), where we stated:

> "It has been repeatedly held that under the 21st Amendment a state may absolutely prohibit the manufacture, transportation, importation, sale or possession of alcoholic liquors irrespective of when or where

> produced or obtained, or the use to which they are to be put, and may adopt measures reasonably appropriate to effectuate those inhibitions and exercise full police authority in respect to them, unfettered by the due process clause, the equal protection clause or the commerce clause."

These general principles were followed in *Laird & Company v. Cheney*, 196 Kan. 675, 414 P.2d 18; and *Tri-State Hotel Co. v. Londerholm*, 195 Kan. 748, 408 P.2d 877 (1965).

It is argued by appellees that this court deviated from those rules in *City of Baxter Springs v. Bryant*, 226 Kan. 383, 598 P.2d 1051. We do not agree with that rationale. *City of Baxter Springs* involved a suit by the city against the proprietor of a local disco for violation of city ordinances prohibiting dispensing of beer and allowing dancing in the disco. In addition, the proprietor was charged with failure to provide an unobstructed view of the premises from the street. We discussed the application of the Twenty-first Amendment in considering the constitutionality of the city ordinances which pertained to regulation of establishments serving cereal malt beverages. The court held the ordinances unconstitutional because they were not "reasonably calculated to promote the health, sanitation, morals, or general welfare of the residents of Baxter Springs. . . ." *City of Baxter Springs v. Bryant*, 226 Kan. at 392, 598 P.2d at 1059. The central issue before the court in that case was the regulation of certain types of activity in or around an establishment that dispensed cereal malt beverages. This court found a state may not, under color of the Twenty-first Amendment, impinge upon individual

rights protected by the Due Process and Equal Protection clauses. See *Craig v. Boren*, 429 U.S. 190, 97 S.Ct. 451. The case did not, however, deal directly with the state's broad authority to regulate the manufacture, distribution, sale, possession and consumption of alcoholic liquor. We find that regulatory power was not modified or lessened in *City of Baxter Springs.*

In addition to the weight of authority, both federal and state, which supports the broad regulatory power of a state, in the area of alcoholic liquor, we find another rationale for upholding H.B. 2020. The provisions of H.B. 2020 on its face will allow sufficient brand and price competition to withstand allegations of a violation of the Sherman Anti-Trust Act. The law is neutral and provides that any licensed distributor may obtain an exclusive franchise for one or more brand of alcoholic liquor from any licensed manufacturer for any designated area of the state. There are eight distributors, 14 categories of liquor, approximately 80 manufacturers, and well in excess of the 260 brands of alcoholic liquor initially referred to in trial exhibits, each of which is subject to a separate franchise. On its face, that would appear to present ample opportunity for each to exercise its own perseverance to obtain products and territory. If one or more fails to obtain its share of the market the law is not at fault; it is one of the hazards of a free market.

Although appellees introduced testimony showing Standard has 32.33% of the market and Famous has 31.83% of the market, there is no evidence the two companies have together embarked upon a monopolistic venture. Appellees

further admit Colby, Grant-Billingsley and Kansas Distributors jointly agreed to make franchise applications for the same brands, each taking a prearranged portion of the state. This indicates they themselves may have conspired to restrain trade. Nothing in the testimony or exhibits proves H.B. 2020, on its face, provides for a combination in restraint of trade. Mr. Terrell concluded a monopoly would eventually result. We believe we may assume competition presently exists and will continue. Should any manufacturer, distributor or combination thereof conspire to restrain trade, the anti-trust laws are available as a remedy.

By allowing the liquor price to seek its own level at the second tier of the liquor system, the legislature has released liquor pricing from its former status as a totally controlled commodity. The price is no longer totally regulated, totally fixed and can now fluctuate as the competition in the market place will determine. With respect to exclusive franchising, we have noted there are now at least two distributors operating in every area of the state. Each distributes different brands, which compete with one another. Although each distributor completely controls the distribution of its brands within its territory we find the competition among brands to be sufficient to withstand claims of restraint of trade. We are urged by appellees to consider the recent California cases of *Midcal Aluminum, Inc. v. Rice*, 90 Cal.App.3d 979, 153 Cal.Rptr. 757 (1979), and *Rice v. Alcoholic Bev. etc. Appeals Bd.*, 21 Cal. 3d 431, 146 Cal.Rptr. 585, 579 P.2d 476 (1978). *Rice* struck down California price maintenance statutes as a violation of policies of the Sherman Anti-Trust Act. while *Midcal*

Aluminum, Inc. struck down fair trade and wine price posting provisions of the California Alcoholic Beverage Control Act, as violative of the Sherman Act. We have carefully considered these cases and find them contrary to our law and without precedent in Kansas.

We now turn to appellees' specific constitutional arguments. Appellees argue they are denied due process because they are denied the right to continue a lawful occupation. In addition, they argue the Act creates classifications which have no rationale, real or substantial relationship to public safety, health, general welfare or legislative purpose in violation of the Fourteenth Amendment of the U.S. Constitution and sections 1 and 2 of the Bill of Rights of the Kansas Constitution. From our examination of the Act, we discern no such classifications or denial of the right to continue operating. All distributors are eligible to franchise any brand with state-wide territory or less. Nothing in the law denies a distributor the right to pursue liquor wholesaling. The legislature enacted legislation permitting exclusive brand franchising comparable to franchises in other industries. The size of the franchise territory and the designation of the brands are left to private agreement under the best traditions of a free society. The stated legislative purpose is to introduce competition into the pricing of liquor to the public, thereby promoting the public welfare and stopping illegal liquor traffic from out of state by offering a more competitive price. There is nothing before us to show the stated purpose is not working. The appellees' complaint is an economic one over which this court has little control. As the court stated in

Seagram & Sons v. Hostetter, 384 U.S. at 47, 86 S.Ct. at 1262:

> "[I]t is not 'the province of courts to draw on their own views as to the morality, legitimacy, and usefulness of a particular business in order to decide whether a statute bears too heavily upon that business and by so doing violates due process. Under the system of government created by our Constitution, it is up to legislatures, not courts, to decide on the wisdom and utility of legislation.'"

See also *State ex rel. Schneider v. Kennedy*, 225 Kan. at 21, 587 P.2d 844.

Appellees' final point is that sections 2 through 11 and section 14 of H.B. 2020 are unconstitutional because they provide for an impermissible delegation of legislative authority to private persons in violation of Article 2, section 1 of the Kansas Constitution. They cite *Quality Oil Co. v. du Pont & Co.*, 182 Kan. 488, 323 P.2d 731, in support of the argument. *Quality* is distinguishable from the instant case. There, this court considered the Kansas Fair Trade Act which authorized a trademark owner to contract with one retailer for a minimum retail price for a named brand commodity and all retailers were bound thereby with notice. The non-signers were bound by the price agreement even though they were not parties to the contract. It left to the trademark owner the determination of whether or not a minimum price would be imposed upon which commodities and the amount. Here, the legislature determined it would not regulate wholesale prices but would let them seek their level in the competition of the market place. We understand this technique to be tradi-

tional in the capitalist society and thought by most to be the best method of determining a fair market price as long as competition is present. It is difficult to comprehend the logic of how a purposeful legislative decision to remove regulation can be transformed to the unlawful delegation of authority to regulate.

H.B. 2020 reflects the legislature's determination that a minimum price was necessary to insure an orderly market and to promote temperance and that it should be determined by the competition among wholesalers plus a minimum markup determined by the ABC Board of Review from the formula furnished by the legislature. This constitutes a permissible delegation of the ministerial act of administering the pricing regulation with a clear cut guideline. In *Laird & Company v. Cheney*, 196 Kan. 675, 414 P.2d 18, we held fixing wholesale liquor prices at the lowest price for which the item is sold anywhere in the United States was not violative of the commerce clause, the due process or equal protection clauses of the Fourteenth Amendment or comparable sections of the Kansas Constitution. Such practice is completely parallel to the method authorized in H.B. 2020.

We hold pursuant to the power and authority granted the state by the Twenty-first Amendment and pursuant to Article 15, § 10 of the Kansas Constitution, to promote temperance and for the protection of the general welfare, health and safety of the people of Kansas, the legislature properly acted to permit a system of exclusive brand franchises for distributors of alcoholic liquor in Kansas for the purpose of introducing competitive pricing into the

middle tier of the Kansas liquor distribution system and in passing the results of the competition onto the consumer through the retailer at not less than the competitive price, plus minimum markup. We hold Chapter 153 of the 1979 Session Laws of Kansas, known as H.B. 2020, a wholly constitutional enactment of the legislature.

The judgment of the trial court is affirmed in part and reversed in part in conformity with this opinion.

FROMME, J., not participating.

Appendix B

In the Third Judicial District

District Court, Shawnee County, Kansas

Case No. 79-CV-896

[August 31, 1979]

Colby Distributing Co., Inc., et al.,
Plaintiffs,

vs.

Michael C. Lennen, et al.,
Defendants.

MEMORANDUM OPINION

This is an action filed by three wholesalers (distributors) against the Secretary of Revenue, the Director of Alcohol Beverage Control and members of the Alcoholic Beverage Control Board of Review of the State of Kansas seeking a declaratory judgment and permanent injunction from the enforcement of House Bill No. 2020, enacted by the state legislature, effective May 10, 1979.

The plaintiffs are licensed distributors of alcoholic liquor in accordance with the Kansas Liquor Act, pursuant to K.S.A. 1978 Supp. 41-103(8), 41-306 and 41-311. The intervenors are four licensed distributors, Standard Liquor Corporation, A-B Sales, Inc.; Sunflower Sales Company; and Eastern Distributing Company; the District Attorney of Sedgwick County, Kansas; and the Kansas Retail Liquor Dealers Association as amicus.

The defendants are the duly qualified agencies who regulate and enforce the liquor laws of Kansas.

The case was tried to the Court on August 6 and 7, 1979 and then taken under advisement pending briefs of the parties. The Court is most grateful to counsel for all parties for their diligence and assistance in submitting most thorough and exhaustive briefs to assist the Court on a matter of first impression before the Kansas Courts.

The issue before the Court is the legality of portions of H.B. 2020 as they pertain to the creation of exclusive franchising between the suppliers (distillers) of alcoholic liquor and the distributors and the change from fixing minimum prices on liquor sold by distributors and licensed retailers to the removal of this price fixing over the distributor and the setting of minimum mark-ups over the retailers, as specifically set out herein below.

A cursory background is in order here. In 1949, Kansas enacted the Kansas Liquor Control Act (K.S.A. 41-101 et seq.) which provides for the regulation of all phases of the manufacture, distribution, sale, possession and consumption of alcoholic liquor. Except for 1965 and again in 1978 (Private Club Act and Restaurant Club Act) the Act has been virtually unchanged.

Kansas has the three-tier system whereby the supplier (manufacturer) can only sell to the distributor (wholesaler) who can only sell to the retailer; none can own any interest in the other and all are licensed by the state.

Prior to the enactment of H.B. 2020, the liquor act provided only for "open wholesaling", prohibiting exclusive distributorship arrangements. It required suppliers to sell

to all distributors at the lowest prices they sell in other states. Distributors were required to sell to all licensed retailers on an equal basis. The minimum sales prices for liquor at wholesale and retail was established by the ABC Board of Review, allowing for mark-ups permitted to both. House Bill 2020 replaced the open wholesaling system for [sic] an exclusive franchise system which grants territories to the distributors to wholesale alcoholic liquor and eliminated regulation of minimum prices for distributors and retailers, providing for minimum mark-ups by retailers.

Sections K.S.A. 41-407, 41-1111, 41-1113, 41-1114, 41-1115 and 41-1117, and K.S.A. 1978 Supp. 41-306, 41-701, 41-719, 41-1101 and 41-1116 were amended and 41-1113 was repealed.

Under attack are the following:

Section 2, amending K.S.A. 1978 Supp. 41-306

Section 3, new section

Section 4, amending K.S.A. 1978 Supp. 41-701

Section 5, amending K.S.A. 1978-Supp. 41-1101

Section 6, amending K.S.A. 41-1111

Section 7, amending K.S.A. 41-1114

Section 8, amending K.S.A. 41-1115

Section 9, amending K.S.A. 1978 Supp. 41-1116

Section 10, amending K.S.A. 41-1117

Section 11, new section

Section 14, amending and repealing the above.

With this background the Court makes the following findings of fact, conclusions of law and decision:

FINDINGS OF FACT

1. In substance, the pertinent portions of the Act provide as follows:

a. Sec. 2 allows distributors to sell only such brands of alcoholic liquor to only those retailers whose licensed premises are located within the geographic territory for which such distributor is authorized to sell such brand as designated in the notice or notices filed with the Director pursuant to Sec. 3;

b. Sec. 3 prohibits any distributor from selling any alcoholic liquor in this state unless such distributor has filed with the Director a written notice stating each geographic territory as has been agreed upon between such distributor and a distiller within which such distributor shall sell to retailers one or more brands of such distiller. Said section further provides that no distiller shall grant such a franchise for the distribution of a brand to more than one distributor for all or part of any designated territory. Said section likewise prescribes and limits in sub-sections (3), (4), (5) and (6) the ability of any such distiller or such distributor to terminate or modify any such franchise or to alter the geographic territory designated in such franchise agreement, except for reasonable cause;

c. Sec. 4 prohibits any distributor of alcoholic liquor from selling a brand or kind of such liquor to any retailer whose licensed premises are located outside said distributor's exclusive franchise territory for such brand as established under Sec. 3 described hereinabove. Sec. 4 further prohibits any distiller or

distributor from fixing, maintaining, coercing or controlling the resale price of such alcoholic liquor to be resold by such distributor or distiller, but specifically authorizes distributors to furnish licensed retailers with a price list of the retail minimum price, including the minimum mark-up, for all such liquor sold by such distributors to such retailers;

d. Sec. 5 prohibits any distributor of alcoholic liquor from purchasing any such liquor from any distiller unless such distiller shall file with the Director a written statement agreeing to sell any of the brands or kinds of such liquor manufactured and distributed by such distiller to any distributor licensed in this state and having a franchise to distribute such brands of such liquor, pursuant to Sec. 3, and to make such sales to all franchised distributors at the same current price and without discrimination and to file periodic price lists showing their current prices with the office of the Director. Sec. 5 further prohibits any licensed retailer from purchasing any such liquor from any such distributor unless such distributor shall file with the Director a written statement agreeing to sell any of the brands or kinds of such liquor distributed by such distributor and to provide service in connection therewith to any licensed retailer whose licensed premises are located within the geographic territory of such distributor's franchise for such liquor, to make such sales to all such licensed retailers at the same current bottle and case price, and without discrimination and to file price lists showing such current bottle and case price in the office of the Director periodically;

e. Sec. 6 sepcifically [sic] provides that the sales price of alcoholic liquor sold by distiller to licensed distributors of alcoholic liquor shall be no higher than the lowest price for which same is sold to distributors anywhere in the continental United States, and that the minimum mark-ups of such liquor to be sold by retailers licensed in this state should be determined and regulated by the ABC Board and thereby eliminates from any regulation whatsoever the price at which such liquor can be sold by distributors to retailers and the minimum price at which such liquor can be sold by retailers to consumers[;]

f. Sec. 7, Sec. 8, Sec. 9 and Sec. 10 deal with the establishment of ABC board of minimum mark-up which shall be charged by retailers in sales of alcoholic liquor to consumers;

g. New Sec. 11 provides for a period of 120 days or until September 10, 1979, wherein a presently licensed distributor, such as the Plaintiffs herein, may sell any alcoholic liquors that such distributor may have on hand at the time this Act takes effect in the same manner, and to the same purchasers as such distributor was authorized to sell the same prior to May 10, 1979.

2. Prior to H.B. 2020, the sale of alcoholic liquor was effected through a three-tier system of distribution, the effect of which was threefold: (1) the distiller was forced to sell to distributors at the lowest distillery price anywhere in the United States; (2) the minimum price charged by the distributor to the retailer was controlled and established by the ABC Board; and (3) the minimum price

which the retailers could charge to the public was likewise established by the ABC Board.

3. The amendments to the Liquor Act by H.B. 2020 drastically change the method of doing business at the distributor level, in that:

a. franchise territories are to be established for each distributor; and

b. each distributor may sell only to those retailers within the newly established franchised territory; and

c. no distiller shall grant a franchise to more than one distributor within the franchised territory; and

d. each distributor is free to establish and post with the ABC any price on any brand of alcoholic liquor of any kind as each distributor may, in his economic wisdom, so determine; and

e. the minimum mark-up, which the retailers are required to charge on all such liquor sold to the consumer public, is fixed by a formula consisting of the following expense items: (1) mean prices posted by distributors, (2) taxes, (3) mean selling costs of retailers, (4) the mean of other reasonable expenses, (5) a reasonable profit to the retailers. This formula is to be established by the ABC pursuant to certain statutory directives.

4. The "minimum mark-up" so established by Sec. 9, H.B. 2020, insofar as it applies to retailers, is essentially the same method used by the ABC Board prior to H.B. 2020. In effect, a percentage mark-up is established and that "mark-up" is applied across the board as to the cost

of merchandise to the retailer, which price will be posted by the distributors as heretofore set out. For example, the present rate of mark-up is 28.5% for all liquor. If a case of scotch whiskey were to be purchased by the retailer for $100, the minimum price to the public for that case would be $128.50. If a distributor desires to post a price of $125 per case of scotch whiskey to the retailer, the retailer's minimum price to the public would be (125 x 1.285) $160.62.

5. Pursuant to H.B. 2020, the distributor is free to change the price which it charges the retailer at any time by posting such price change with the Director. The result of this freedom statutorily granted to the distributor is to allow each distributor to effectively control and determine the minimum price for each brand of liquor for which it has a franchise since neither the Director nor the ABC Board has any regulatory control over the prices charged by the distributor to the retailer. Therefore, the ABC Board, the Director, the retailer, and the public at large all are forced by the statute to abide by the decision of the distributor as to the retail minimum price.

6. The Subject Sections of H.B. 2020, in effect, permit a licensed and franchised distributor of alcoholic liquor to establish the only sales price at which any retailer located within such distributor's franchise territory can purchase any brand or kind of alcoholic liquor that such distributor is franchised to sell. As a result, said distributor is authorized to set a monopoly price upon such brand or kind of alcoholic liquor within such franchise territory which is binding upon all retailers located within such franchise territory.

7. The Subject Sections of H.B. 2020, and, more particularly Sec. 4(4) and Sec. 10, further permit a licensed and franchised distributor of alcoholic liquor to establish the minimum sales price at which all retailers located within such distributor's franchise territory must sell such brand or kind of such liquor to all consumers or retail customers within such franchise territory. As a result, said distributor is authorized, by statute, to fix the minimum resale price on any such brand or kind of alcoholic liquor sold within such franchise territory and, in effect, to force all consumers or retail purchasers of such brand or kind of alcoholic liquor to purchase such liquor at no less than said distributor's minimum retail price.

8. The Liquor Act, as amended by H.B. 2020, removes all authority from the Director and ABC Board to determine or regulate either the price charged for alcoholic liquor by distributors to retailers, or the minimum price which must be charged by retailers to consumers for such liquor. Said Act contains no standards governing the determination of such prices by such franchised distributor nor does said Act contain any procedure whereby said Director or said ABC Board can determine the reasonableness of such prices.

9. The Act, as amended by H.B. 2020 and, more particularly, sections 2, 3, 4 and 5, permit a licensed distiller and a licensed distributor to establish a geographic franchise territory for the exclusive sale of one or more brands or kinds of alcoholic liquor of such distiller by such distributor, and prohibit the sale of such brand or kind of such liquor within such territory by more than one such

distributor. Said sections further permit one licensed distributor to establish such franchises for more than one brand or kind and with more than one distiller and, thereby, preclude all other licensed distributors from selling all such brands or kinds of such liquor of such distillers within such franchised territories. As a result, said franchised distributors and said distiller are authorized to create a monopoly in the distribution and sale of such brand or kind of alcoholic liquor in a geographic area which may be, if the parties so choose, as large as the entire state of Kansas. Furthermore, any one licensed distributor is permitted to establish such a monoploy [sic] in as many brands or kinds of alcoholic liquor of as many distillers as shall agree to franchise such distributor. As a result, one distributor is permitted to establish a franchise monopoly for a geographic territory as large as the state of Kansas, and to establish such a monopoly in as many brands or kinds of alcoholic liquor of as many distillers as such distributor may desire, and thereby preclude and prevent all other licensed distributors from engaging in the distribution of all such brands or kinds of such liquor.

10. The Act, as amended by H.B. 2020, contains no standards by which the geographic size or the number of such monopoly franchises may be measured, determined or limited, and the Director and the ABC Board are given no authority to determine the reasonableness of the size of such franchised territories nor to regulate or limit the number of such monopoly franchises which may be obtained by any one licensed distributor.

CONCLUSIONS OF LAW

1. This Court has jurisdiction over the subject matters here notwithstanding the issues as framed concern federal questions and interpretation of federal laws as they may apply to state laws.

2. H.B. 2020, and, more particularly, Sec 4(4) and Sec 10, permit a licensed and franchised distributor of alcoholic liquor to establish the minimum sales price at which all retailers located within such distributor's franchised territory must sell such brand or kind of such liquor to all consumers or retail customers. Such resale price maintenance by franchised and licensed distributors violates Section 1 of the Sherman Act (15 U.S.C. § 1).

3. (a) It is true that the twenty-first Amendment of the U.S. Constitution created an exception to the normal operation of the Commerce Clause but consistently the federal courts have held that the Twenty-first Amendment does not pro tanto repeal the Commerce Clause, but merely requires that each provision be considered in the light of each other. The Sherman Act derives its authority from the Commerce Clause. Neither does this amendment prevail over other provisions of the Constitution where the regulation or law of the state in the field of alcoholic beverages tends to be discriminatory. See City of *Baxter Springs vs. Bryant*, # 50,747, opinion filed August 9, 1979.

(b) Is a violation of the Sherman Act, which this Court has found, saved by the Twenty-first Amendment? If the state through H.B. 2020 imposed price fixing throughout the three tiers, a valid argument may be made that the state may prescribe and fix prices for resale in intrastate

commerce in contravention of [the] Sherman [Act]. But here, the distributor, not the state controls the ultimate price the consumer pays. The state regulates the retailer's pricing, as required in sections 7, 8, 9 and 10, but the cost to the retailer in the purchase of liquor from the distributor is a prime factor in establishing ultimate price paid by the consumer. Where a private person or persons has the discretion to set the price an attempt by the state as contemplated in H. B. 2020 to regulate resale price is illegal as a violation of the Sherman Act. The state does not participate in determining the minimum price to be charged by the distributor. In essence, the statute permits the distributor to engage in resale price maintenance and to control the dollar volume of the mark-up. In addition, this provision constitutes an attempt by [sic—presumably the words "to delegate" should be substituted for "by"] the legislative power to control pricing, which is illegal. *Quality Oil Co. v. Dupont & Co.*, 182 Kan. 488, 322 P. 2d 731.

(c) Reference has been made to the twenty-first Amendment and the Sherman Act. In essence, they respectively provide:

> "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited" (Twenty-first)
>
> "Every contract, combination in the the [sic] form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states . . . is hereby declared to be illegal" (Sherman Act)

4. The state has the right to establish and regulate franchise areas under the police power to regulate the

liquor industry so long as these laws do not interfere [with] or impede valid federal law or constitutional safeguards. Providing for suppliers and distributors to establish exclusive franchise areas without state intervention or state power to control or regulate has no reasonable rational relation to the purpose of fostering temperance and orderly marketing conditions. The effect of the exclusive franchise system authorizes private persons to engage in anti-competitive conduct and constitutes a violation of the Sherman Act.

5. It is even more pernicious to allow price fixing with an exclusive franchise to sell, both controlled by the same non-government entity, without regulation by the state.

6. The proposed exclusive franchise does not tend to preserve public health, safety or welfare but has a tendency to stifle legitimate business by creating a monopoly or trade barrier, in violation of the Sherman Act and is unconstitutional as an invasion of the property rights of the individual.

7. The beneficial purpose of these amendments that prices to the consumer will be lowered is insufficient when gauged by constitutional deficiencies.

8. The state alludes to the preservation of the three-tier system but in fact, the balance is upset when one of the entities, here the distributor, is clothed with sole and discretionary resale price maintenance coupled with an exclusive franchise to sell certain alcoholic liquor. In no way is this Court inferring that any distributor will nefariously employ this new statute to his gain and to the detriment

of the public good. Even proof that prices will be reasonable and the retailer will end up with better service from the distributor are not sufficient to uphold resale price fixing and exclusive franchise. The point here is that they are contrary to public policy and even the good will and intent of the distributors are not sufficient to overcome this deficiency. Nor is the statute saved because they are performed under complusion [sic] of law.

9. The Court is well aware of the ramifications of its decisions declaring price fixing and exclusive franchising as void. The effect may very well presume open and free competition and pricing as in other commercial endeavors. (Note the Special Committee's suggestion that removal of retail price control may be considered in the future.) (Proposal No. 16).

Until the legislature convenes next January, there is adequate law on the books to allow for control and regulation of the liquor industry. There is a savings provision in H.B. 2020 (section 12).

10. To insure an orderly marketing condition and create the least chaos until January of 1979, the Court's decision and findings on the issue of franchising as being invalid is directed solely to "exclusive franchising". The Court finds that providing for a franchise system permitting all distributors to participate in obtaining territories and engaging in intrabrand competition does not constitute a violation of [the] Sherman [Act], is not anti-competitive nor cause any chilling effect on federal or state law. The legislature will have to be the final judge of the wisdom of non-exclusive franchising.

11. Further, in the decision that resale price maintenance is invalid, the compelling interest of the state is more apparent in regulating supplies and distributors in the orderly business of transporting into the state and in the wholesale distribution of liquor to the retailer.

Therefore, the following sections are declared void in accordance with these findings, conclusions and decisions:

a. Section 7

b. Section 8

c. Section 9

d. Section 10

12. The following sections are valid except as follows:

a. New section 3(1)—Delete "No manufacturers, importer or other supplier shall grant a franchise for the distribution of a brand to more than one distributor for all or part of any designated territory."

b. Section 6 –Delete "and (b) that minimum mark-ups on alcoholic liquor sold by retailers licensed in this state should be determined and regulated by law".

c. Section 10(2)—Delete "plus minimum mark-up".

All other sections are valid.

13. By striking all reference to exclusiveness of franchises, each of the nine Kansas distributors is free to negotiate with the suppliers and manufacturers for a territory they can best serve. This would allow for intrabrand competition between distributors and only require the distributor to have in inventory those brands it can sell under its franchise as compared with the old law requiring full inventory of all brands.

14. The present Act requires the supplier to sell to distributors at a price no higher than the lowest price the item is sold in the U.S. (Section 6). It requires the distributor to sell to the retailer at the same current bottle and case price without discrimination (Section 5(2)). The retailer may not sell any liquor at less than its current posted bottle cost (Section 10(2)). The prohibition against inducements, et cetera is still preserved in Chapter 41, Article 7.

Plaintiffs are granted permanent injunction restraining and enjoining the defendants, their officers, agents and employees from implementing and enforcing those portions of H.B. 2020 consistent with this decision.

This decision is effective this 31st day of August, 1979.

/s/ MICHAEL A. BARBARA
Michael A. Barbara
District Judge, Div. II

Appendix C

In the Supreme Court of the State of Kansas

No. 51,428

Colby Distributing Co., Inc., et al
Appellee

v.

Michael C. Lennen, et al
Appellants

You are hereby notified of the following action taken in the above entitled case:

Motion for Rehearing.

Considered and DENIED.

Yours very truly,

Lewis C. Carter
Clerk, Supreme Court

Date April 9, 1980

Appendix D

In the Supreme Court of the State of Kansas

Case No. 51,428

Grant-Billingsley Wholesale Liquor Company, Inc.,
Appellant,

vs.

Michael C. Lennen, et al.,
Appellees.

[Filed June 25, 1980]

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Grant-Billingsley Wholesale Liquor Company, Inc., the appellant above-named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of Kansas, in the case of Colby Distributing Co., Inc., et al., Plaintiffs-Appellees and Cross-Appellants, v. Michael C. Lennen, et al., Defendants-Appellants, bearing the above captioned case number. The judgment of the Supreme Court of the State of Kansas hereby appealed was subject to a timely petition for rehearing, which that Court denied on April 9, 1980, with mandate issuing on April 21, 1980.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

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[Certificate of Service Omitted in Printing]

In the Third Judicial District

District Court, Shawnee County, Kansas
Civil Department

Case No. 79 CV 96

Grant-Billingsley Wholesale Liquor Company, Inc.,
Appellant,
vs.
Michael C. Lennen, et al.,
Appellee.

[Filed June 25, 1980]

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Grant-Billingsley Wholesale Liquor Company, Inc., the appellant above-named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of the State of Kansas, in the case of Colby Distributing Co., Inc., et al., Plaintiffs-Appellees and Cross-Appellants, v. Michael C. Lennen, et al., Defendants-Appellants, bearing the case number of 51,428. The judgment of the Supreme Court of the State of Kansas hereby appealed was subject to a timely petition for rehearing, which that Court denied on April 9, 1980, with mandate issuing on April 21, 1980.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

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Appendix E

HOUSE BILL No. 2020

An Act amending and supplementing the Kansas liquor control act; providing for a territorial franchise system on distribution of certain alcoholic liquors; eliminating the regulation of minimum prices of distributors and retailers; providing for minimum mark-ups by retailers; allowing removal of alcoholic liquor from bonded warehouses between sunset and sunrise; removing certain prohibitions against the consumption of alcoholic liquors in certain places amending K.S.A. 41-407, 41-1111, 41-1114, 41-1115 and 41-1117 and K.S.A. 1978 Supp. 41-306, 41-701, 41-719, 41-1101 and 41-1116 and repealing the existing sections; also repealing K.S.A. 41-1113.

Be it enacted by the Legislature of the State of Kansas:

• • • • • • • • •

Sec. 2. K.S.A. 1978 Supp. 41-306 is hereby amended to read as follows: 41-306. An alcoholic liquor distributor's license, except a beer distributor's license, shall allow: (1) The wholesale purchase, importation, *and* storage ~~and sale~~ of alcoholic liquors, except beer, ~~to licensees in this state and to such persons without the state as may be permitted by law~~, but all such alcoholic liquor so purchased or imported which is manufactured in the United States shall be purchased from the primary American source of supply or from another licensed distributor, except that a licensed distributor may purchase confiscated alcoholic liquor at a sheriff's sale; ~~and~~

(2) The sale of alcoholic liquors, except beer, to:

(a) Distributors licensed in this state,

(b) Retailers licensed in this state, except that a licensed distributor shall sell a brand of alcoholic liquor only to those retailers whose licensed premises are located in the geographic territory within which such distributor is authorized to sell such brand, as designated in the notice or notices filed with the director pursuant to section 3, and

(c) Such persons located outside such territory or outside this state as permitted by law;

(3) The purchase of alcoholic liquors, except beer, in barrels, casks or other bulk containers and the bottling thereof before resale, but all bottles or containers filled with such alcoholic liquors shall be sealed, labeled, stamped and otherwise made to comply with all laws and rules and regulations governing the preparation and bottling of alcoholic liquors by manufacturers and with all federal rules, regulations and laws.

New Sec. 3. (1) No distributor of alcoholic liquor, except beer, shall sell any alcoholic liquor in this state unless such distributor has filed with the director a written notice stating each geographic territory, agreed upon in writing between the distributor and a supplier of the distributor, within which the distributor sells to retailers one or more brands of such supplier. Such notice shall be accompanied by a map outlining each geographic territory stated in the notice. No manufacturer, importer or other supplier shall grant a franchise for the distribution of a brand to more than one distributor for all or part of any designated territory.

(2) Each supplier of alcoholic liquors doing business within this state shall file with the director a written notice describing each geographic territory, agreed upon in writing between the supplier and a distributor, within which the distributor sells to licensed retailers one or more brands of the supplier.

(3) No supplier or distributor shall terminate or modify a franchise for the distribution of a brand of alcoholic liquor or alter the geographic territory designated in a franchise agreement unless such supplier or distributor files written notice thereof with the director not less than thirty (30) days prior to the termination, modification or alteration. In the case of an alteration [of] a franchise territory, such notice shall be accompanied by a map outlining the altered territory. Upon receipt of such notice, the director shall notify immediately, by certified mail, all affected parties of the impending termination, modification or alteration.

(4) Any notice filed by a supplier pursuant to subsection (3) shall be accompanied by an affidavit stating that the termination, modification or alteration is not caused by the failure of the distributor to violate any provision of the Kansas liquor control act or any rules and regulations adopted pursuant thereto.

(5) Any supplier or distributor aggrieved by a termination, modification or alteration made under subsection (3) may file an appropriate action in any district court of this state having venue, alleging that the termination, modification or alteration violates the franchise agreement between the supplier and distributor involved.

(6) No franchise agreement for the distribution of a brand of alcoholic liquor shall be terminated or modified, nor shall the territory designated in such an agreement be altered, except for reasonable cause.

(7) This section shall be part of and supplemental to the Kansas liquor control act.

Sec. 4. K.S.A. 1978 Supp. 41-701 is hereby amended to read as follows: 41-701. *(1)* No distributor or wholesaler shall sell or attempt to sell any alcoholic liquor within this state except to:

(a) A licensed manufacturer, licensed nonbeverage user or licensed distributor: ~~*Provided*, That a licensed distributor may sell or attempt to sell alcoholic liquor within this state to;~~ *or*

(b) A licensed retailer, except that, *subject to the provisions of subsection (2):*

(i) No distributor of alcoholic liquor, except beer, shall sell a brand of alcoholic liquor to any retailer whose licensed premises are located outside of the geographic territory within which such distributor is authorized to sell such brand, as designated in the notice filed with the director pursuant to section 3; and

(ii) No beer distributor shall sell beer to any retailer who is located outside the geographic territory designated in the notice filed with the director by the distributor pursuant to K.S.A. *1978 Supp.* 41-409-, ~~as amended: *Provided*, That~~

(2) (a) If any beer distributor ~~shall refuse~~ *refuses* to sell beer or provide service in connection therewith to any retailer located within such beer distributor's geo-

graphic territory, it shall be lawful for any other beer distributor to sell beer to such retailer.

(b) If any licensed distributor of alcoholic liquor, except beer, refuses to sell alcoholic liquor which such distributor is authorized to sell or refuses to provide any service in connection therewith to any retailer located within such distributor's geographic territory, it shall be lawful for any other licensed distributor of alcoholic liquor, except beer, to sell such liquor to such retailer

(3) No manufacturer of alcoholic liquor shall sell or attempt to sell any alcoholic liquor within this state except to a licensed manufacturer, licensed distributor or licensed nonbeverage user: ~~*Provided,*~~ *except* that the holder of a license to manufacture beer may also attempt to sell or sell beer manufactured by ~~him~~ *such manufacturer* to retailers licensed in this state: ~~*Provided further, That,*~~ *but* a licensed manufacturer of beer shall not sell or attempt to sell any beer manufactured by ~~him~~ *such manufacturer* containing not to exceed three and two-tenths percent (3.2%) of alcohol by weight to any person in this state other than a wholesaler or distributor licensed as such under the laws of this state relating to cereal malt beverages and malt products.

(4) No *supplier*, wholesaler, distributor, manufacturer or importer shall by oral or written contract or agreement, expressly or impliedly fix, maintain, coerce or control the resale price of *alcoholic liquor*, beer or cereal malt beverage to be resold by such wholesaler, distributor, manufacturer or importer, *except that a licensed distributor may furnish to retailers lists of the minimum bottle and case prices*

required under subsection (2) of K.S.A. 41-1117 and amendments thereto.

(5) **Any *supplier,* wholesaler, distributor or manufacturer violating the provisions of this section shall be guilty of a misdemeanor and upon conviction thereof shall be punished by a fine of not less than five hundred dollars ($500) and not more than one thousand dollars ($1,000), to which may be added not to exceed six (6) months imprisonment ~~and~~. In addition, any *supplier,* wholesaler, distributor, manufacturer or importer violating the provisions of this section relating to fixing, maintaining or controlling the resale price of *alcoholic liquor,* beer or cereal malt beverage shall be liable in a civil action to treble the amount of any damages awarded plus reasonable attorney fees for the damaged party.**

Sec. 5. K.S.A. 1978 Supp. 41-1101 is hereby amended to read as follows: 41-1101. (1) It shall be unlawful for any distributor licensed under this act to purchase any alcoholic liquor from any manufacturer, owner of alcoholic liquor at the time it becomes a marketable product, exclusive agent of such manufacturer or owner or distributor of alcoholic liquor bottled in a foreign country either within or without this state, unless such manufacturer, owner, exclusive agent or distributor shall file with the director a written statement sworn to by such manufacturer, owner, exclusive agent or distributor or, in case of a corporation, one of its principal officers, agreeing to sell any of the brands or kinds of alcoholic liquor manufactured or distributed by such manufacturer, owner, exclusive agent or distributor to any distributor licensed in this state *and having a franchise to distribute such alcoholic liquor pur-*

suant to section 3, to make such sales to all *such* licensed distributors in this state at the same current price and without discrimination and to file price lists showing the current prices in the office of the director as often as may be necessary or required by the director but at least once each three months. If any manufacturer, owner, exclusive agent or distributor making such agreement violates such agreement by refusing to sell *such alcoholic liquor* to any *such franchised* licensed distributor in this state or discriminates in current prices among such *franchised* licensed distributors making or attempting to make purchases of alcoholic liquor from such manufacturer, owner, exclusive agent or distributor, the director shall notify, by registered mail, each *such franchised* licensed distributor in this state of such violation. Thereupon, it shall be unlawful for *such* a *franchised* licensed distributor in this state to purchase any alcoholic liquor from such manufacturer, owner, exclusive agent or distributor. If thereafter *such* a *franchised* licensed distributor shall purchase any alcoholic liquor from such manufacturer, owner, exclusive agent or distributor such *franchised* licensed distributor's license shall be revoked by the director If any manufacturer, owner, exclusive agent or distributor of alcoholic liquor bottled in a foreign country making any agreement hereunder shall not have a sufficient supply of alcoholic liquor of any of the brands or kinds which such manufacturer, owner, exclusive agent or distributor manufactures or distributes to supply the demands of all licensed distributors *having a franchise to distribute such alcoholic liquor*, such manufacturer, owner, exclusive agent or distributor may ration such alcoholic liquor and apportion the available supply among ~~the~~ *such franchised* licensed distributors purchasing or

attempting to purchase the same, in accordance with a plan which shall be subject to the approval of the director. The provisions of this subsection relating to the filing of price lists with the director shall not apply to any manufacturer with respect to alcoholic liquor manufactured or bottled in a foreign country.

(2) It shall be unlawful for any retailer licensed under this act to purchase any alcoholic liquor from any distributor licensed under this act unless such distributor shall file with the director a written statement sworn to by such distributor, or in case of a corporation by one of its principal officers, agreeing to sell any of the brands or kinds of alcoholic liquor distributed by such distributor *and to provide service in connection therewith* to any *licensed* retailer ~~licensed in this state~~ *whose licensed premises are located within the geographic territory of such distributor's franchise for such alcoholic liquors, unless written approval to do otherwise is obtained from the director;* to make such sales to all such licensed retailers at the same current *bottle and case* price and without discrimination; and to file price lists showing the current *bottle and case* price in the office of the director as often as may be necessary or required by the director but at least once each three months. If any distributor making such agreement violates such agreement by refusing to sell *or provide service* to any *such* licensed retailer in this state *without written approval of the director* or discriminates in current prices among such licensed retailers making or attempting to make purchases of alcoholic liquor from such distributor, the director shall revoke the license of such distributor. If any licensed distributor making any agreement here-

under shall not have a sufficient supply of alcoholic liquor of any of the brands or kinds which such distributor distributes to supply the demands of all *such* licensed retailers such distributor may ration such alcoholic liquor and apportion the available supply among the *such* licensed retailers purchasing or attempting to purchase the same, in accordance with a plan which shall be subject to the approval of the director.

(3) The provisions of this section shall not apply to any distributor of beer or any manufacturer or importer of beer, whether within or without this state, with respect to beer distributed or manufactured by such distributor, manufacurer or importer.

Sec. 6. K.S.A. 41-1111 is hereby amended to read as follows: 41-1111. In the public interest and in order to promote the orderly sale and distribution of alcoholic liquor, to foster temperance and to promote the public welfare, ~~in the state of Kansas~~, the legislature finds: (a) That sales prices of alcoholic liquor sold by manufacturers and others to distributors licensed in this state should be no higher than the lowest price for which the same is sold to distributors anywhere in the continental United States; and (b) that minimum ~~sale prices for~~ *mark-ups on* alcoholic liquor sold by ~~distributors and~~ retailers licensed in this state should be determined and regulated by law.

Sec. 7. K.S.A. 41-1114 is hereby amended to read as follows: 41-1114. The board shall establish ~~and fix minimum prices for which an item of alcoholic liquor may be sold by a retailer licensed in this state~~ *minimum mark-ups*

which shall be charged by retailers on sales of alcoholic liquor to consumers.

Sec. 8. K.S.A. 41-1115 is hereby amended to read as follows: 41-1115. The board, in exercising its powers and duties under the provisions of this act, shall establish ~~and determine: (a) The minimum "case prices" and the minimum "bottle sale prices" from distributor to retailer; and (b) the minimum "case prices," the minimum "bottle sale prices," and the minimum "mixed case sale prices" from retailer to consumer~~ *the minimum mark-up by retailers on sales of cases, bottles and mixed cases to consumers.*

Sec. 9. K.S.A. 1978 Supp. 41-1116 is hereby amended to read as follows: 41-1116. The ~~prices so~~ *minimum mark-ups* established ~~and fixed~~ by the board shall be fair and reasonable to ~~licensed distributors,~~ licensed retailers, and the ultimate consumer. ~~Said prices~~ *Such mark-ups* must be in the public interest and such that they do not unduly stimulate the sale and consumption of alcoholic liquor or tend to disrupt the orderly sale and distribution of alcoholic liquor. The board in establishing ~~and fixing such sales prices~~ *minimum mark-ups* shall take into consideration and be guided by the following: (a) The *mean of* acquisition costs ~~to~~ *of* licensed ~~distributors and~~ retailers. ~~The acquisition costs shall be the "case price" to distributors and the "minimum bottle sale price" to retailers;~~ (b) federal, state, and local taxes and license fees *which are* paid by ~~distributors and~~ retailers ~~which~~ *and* are levied or imposed in connection with their business of ~~distributing or~~ selling alcoholic liquor in this state; (c) *the mean* of selling costs of licensed ~~distributors and~~ retailers; (d) ~~cost of transpor-~~

~~tation to distributors from the F.O.B. shipping point to a base point in the state of Kansas, and delivery charges in connection with the shipment of alcoholic liquor; (e)~~ *the mean of* any legitimate, reasonable expense not hereinbefore specified, incurred in the legal conduct of ~~their~~ *licensed retailers'* businesses ~~as licensed distributors and retailers;~~ and ~~(f)~~ *(e)* a reasonable ~~markup or~~ profit for the licensed ~~distributors and~~ retailers. *The board may base its determination of the mean of retailers' acquisition costs, selling costs and operating expenses on a sampling of retailers generally representative of all retailers in the state.* To insure that ~~licensees~~ *retailers* in this state receive only a reasonable markup and profit, the alcoholic beverage control board of review, within ~~a reasonable time~~ *six (6) months* after the effective date of this act, shall conduct *and complete* studies to determine whether the present minimum mark-ups prescribed for ~~licensed distributors and~~ licensed retailers should be *maintained as currently established*, increased or decreased. *Until such studies are completed, the minimum mark-ups in effect immediately prior to the effective date of this act shall remain in effect.*

Sec. 10. K.S.A. 41 1117 is hereby amended to read as follows. 41-1117. *(1)* Whenever the board shall establish ~~and fix minimum distributor or~~ minimum retailer ~~sales prices~~ *mark-ups*, it shall immediately file a copy thereof with the director The director, ~~from time to time, and~~ at least once in each quarter of each year, shall publish ~~the prices so determined and fixed,~~ *such minimum mark-ups* and shall promptly mail a copy to each licensed distributor and retailer ~~and each supplier~~ authorized to do business in this state. ~~All manufacturers and others who have~~

~~filed their prices with the director and board shall be chargeable with a reasonable fee for the printing and mailing of the prices published by the director. Such prices~~ *Minimum mark-ups* shall become effective at twelve (12) o'clock midnight ~~of~~ *on the last day of the first calendar month commencing after the seventh* (7th) day following the day ~~the same~~ *such mark-ups* are mailed to licensed ~~distributors and~~ retailers. ~~On and after the effective date of said minimum sales prices,~~

(*2*) No ~~distributor~~ or retailer shall sell, directly or indirectly, any alcoholic liquor ~~listed in the then currently effective applicable schedule of minimum sales prices as published by the director~~ at less than its ~~listed price~~ *current posted bottle cost plus minimum mark-up* without first having obtained from the director a permit so to do; and the director is authorized to issue such a permit in the following cases:

~~(a) Where the item of alcoholic liquor was actually possessed by the distributor or retailer prior to the effective date of the initial fixing of the minimum sales price of the item;~~

~~(b)~~(*a*) where the ~~distributor or~~ retailer is actually closing out his *or her* stock for the purpose of completely discontinuing sale of such item of alcoholic liquor for a period of not less than twelve (12) months;

~~(c)~~(*b*) where the item of alcoholic liquor is damaged or deteriorated in quality and notice is given to the public thereof; or

~~(d)~~(c) where the sale of the item of alcoholic liquor is by an officer acting under the order of any court.

New Sec. 11. (1) Notwithstanding any contrary provision of this act, for a period of one hundred twenty (120) days after this act takes effect a licensed distributor may sell any alcoholic liquors which such distributor may have on hand at the time this act takes effect in the same manner and to the same purchasers as such distributor was authorized to sell the same prior to the effective date of this act.

(2) This section shall be part of and supplemental to the Kansas liquor control act.

New Sec. 12. If any provisions of this act or the application thereof to any person or circumstances is held invalid, the invalidity shall not affect other provisions or applications of the act which can be given effect without the invalid provisions or application, and, to this end, the provisions of this act are severable.

* * * * * * * * *

Appendix F

CONCENTRATION RATIOS FOR SPIRITS SOLD IN KANSAS

Category	Single-Firm Market Share	Two-Firm Market Share	Three-Firm Market Share	Four-Firm Market Share
Rum	90 %	92.2%	93.6%	94.7%
Corn Whiskey	84	94.8	99.9	N/A
Tequila	66.2	79.2	84	87.5
Light Whiskey	65.7	88.7	100	N/A
Blended Whiskey	63.4	86.8	91.5	93.7
Brandy	61	67.9	74.7	80.5
Cordials	58.9	68.2	74	78.8
Cognac	58.4	87.3	93.5	99.4
Rye Whiskey	38.4	76.8	95.4	99.9
Irish Whiskey	38.2	70.2	94.7	97.4
Prepared Cocktails	37	64.1	78.5	92.9
Vermouth	36.4	60.9	82.7	89.7
Canadian Whiskey	36.3	54.8	72.2	86.7
Vodka (80 Proof)	32.4	63.1	69.5	75.5
Vodka (All Proofs)	30	56.6	68.1	73.8
Bonded Bourbon	26.7	50.4	73.3	82
Gin	25.6	45.7	56.4	65.7
Straight Bourbon	18.9	31.8	44	54.3
Scotch	16.8	32.9	44.2	55.5

Source: 1. Kansas Division of Alcoholic Beverage Control "Report Concerning Shipments of Alcoholic Liquors by Classification and Brands from Distillers to Kansas Distributors for Fiscal Year July 1978 through June 1979"; defendants' ex. 1.

2. Kansas Edition of "Beverage News", June 1980.

Supreme Court, U. S.
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No. 80-189

IN THE SUPREME COURT

OF THE

UNITED STATES

Grant-Billingsley Wholesale Liquor Co., Inc.,
Appellant,

v.

Michael C. Lennen, Secretary of Revenue
For The State of Kansas, et al.,
Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF KANSAS

MOTION TO DISMISS OR AFFIRM

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No. 80-189

IN THE SUPREME COURT

OF THE

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Grant-Billingsley Wholesale Liquor Co., Inc.,
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Conclusion 18

QUESTIONS PRESENTED

The Alcoholic Beverage Industry in Kansas operates on the three (3) independent vertical tier system, including suppliers, wholesalers, and retailers; all of whom are licensed private enterprises authorized to do business in the State of Kansas. Kansas is a "license" state as compared with the "monopoly" states in which the state, itself, conducts all or a part of the business of the distribution of alcoholic liquors.

Since 1949 the Kansas law provided for open-wholesaling under which, subject to credit considerations, suppliers sold to all wholesalers. Under the recent statutory amendments L. 1979, Ch. 153, (H.B. 2020), Kansas now provides for distilleries and wineries to enter into written territorial franchise agreements with wholesalers for exclusive territories. House Bill 2020 does permit sales outside of the territory under certain circumstances.

House Bill 2020 promotes interbrand competition. The statute puts no limits on the number of brands or the number or size of territories a wholesaler may contract with a supplier to service. However, preexisting anti-trust provisions of Kansas law govern the activities of this market, just as they govern the activities of other private enterprises. Reference: Kansas Statutes Annotated 50-101 *et seq.* House Bill 2020, provides for alteration in the franchises with thirty (30) days written notice and for reasonable cause (Ref: Kansas Statutes Annotated 41-410(3)).

The Kansas Supreme Court upheld the statute and reversed the Trial Court. The Court in *Colby v. Lennen*, 227 Kan. 179, 606 P.2d 102 (1980) ruled that:

> "1. Pursuant to the Twenty-First Amendment, a state may absolutely prohibit the manufacture, transportation, importation, sale or possession of alcoholic liquors irrespective of when or where produced or obtained, or the use to which they are to be put, and may adopt measures reasonably appropriate to effectuate those prohibitions and excise full police authority in respect to them, unfetered by the due process clause, the equal protection clause or the commerce clause."
>
> 2. The constitutionality of a statute is presumed, all doubts must be resolved in favor of its validity, and before the statute may be stricken down, it must clearly appear the statute violates the constitution."
>
> 3. In determining constitutionality, it is the court's duty to uphold a statute under attack rather than defeat it and if there is any reasonable way to construe the statute as constitutionally valid, that should be done."
>
> 4. In a civil action, the record is examined and it is *held*: The trial court

> erred in holding pertinent sections of House Bill 2020 unconstitutional."

When the United States Supreme Court announced its decision in *California Retail Liquor Dealers Association vs. Midcal Aluminum Company,* 445 U. S. 97, 100 S.Ct. 937, 946 (1980), that case was brought to the attention of the Kansas Supreme Court in connection with a motion for rehearing. The rehearing request was considered, *Midcal* was considered, and no modification of the prior judgment was rendered.

While appellant submits to this court questions assuming and presumed on facts not in the record, as those for consideration--we assert that the singular question presented is whether or not this is an appropriate forum for consideration of the final judgment of the Kansas Supreme Court on the grounds of substantial Federal question inasmuch as the judgment rests on an adequate non-Federal basis.

As administrators of a field of enterprise wrought with the perils of abuse--often a condition found by the courts to be a truism deserving highest consideration--then, if this court rejects our motion, to dismiss or affirm, the issues herein are not those as set forth by appellants, but are rather

> [1] What is the power reserved to the states by the Twenty-First Amendment to the Federal Constitution? Is it a guarantee, as the Court seems to suggest in *Midcal,* when it states:

> "The Twenty-First Amendment grants the states virtually complete control over whether to permit the importation or sale of liquor and *how to structure the liquor distribution system.*" 100 S.Ct. 937 at 946 (1980).

or is it merely an opportunity for the states to prohibit all such traffic within its borders; and

[2] If an anti-trust analysis is to be applied in the instant case, should there not be a complete examination of the actual effect House Bill 2020 has had, and does have on the Kansas market such that the "rule of reason" test as set forth in *Continental T.V., Inc. vs. G.T.E. Sylvania, Inc.*, 388 U. S. 365 (1977), might be applied?

CONSTITUTIONAL AND STATUTORY PROVISIONS

This case involves the following constitutional and statutory provisions, in pertinent part:

1. United States Constitution, Amendment XXI, §2:

> "The transportation or importation into any State, territory, or possession of the United States for delivery or

use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

2. House Bill 2020 (Kansas Liquor Control Act):

The text of H.B. 2020 is set out in the Jurisdictional Statement of Appellants. Complete copies of the Kansas Liquor Control Act, of which it is a part, and Rules and Regulations adopted thereunder have been provided the Clerk of the Court for distribution.

INTRODUCTION

The question of the strength of the Twenty-First Amendment was briefed and argued before the Kansas Supreme Court, and that court ruled on it directly, upholding the state statute. The Kansas Supreme Court also upheld the statute's constitutionality on other grounds; namely that constitutionality of statutes is presumed, all doubts being resolved in favor of validity and that it's the Court's duty to uphold a statute if reasonably possible to do so.

ARGUMENT AND AUTHORITIES

1. *House Bill 2020 raises only a State issue and gives rise to an inquiry related solely to the Twenty-First Amendment to the United States Constitution.*

The provisions of House Bill 2020 which authorize the designation of exclusive wholesalers and allocated

territories to each wholesaler should be facially reviewed as to whether or not it is a proper exercise under the Twenty-First Amendment to the United States Constitution. The Kansas Supreme Court determined that it was. The designation of wholesalers and territories under this law falls within the express language of the Twenty-First Amendment. This Court as recently as March 1980, commented upon the Twenty-First Amendment and with respect to §2 of that Amendment stated:

> "The Twenty-First Amendment grants the states virtually complete control over whether to permit the importation or sale of liquor and how to structure the liquor distribution system." *California Retail Liquor Dealers Association vs. Midal Aluminum Company*, 445 U. S. 97, 100 S.Ct. 937, 946 (1980).

In a post opinion letter dated March 10, 1980, and signed by attorney Jack B. Owens, Attorney for *Midcal* (who is also counsel for record on behalf of appellant in this cause) to the Honorable Lewis F. Powell, Jr., it was suggested *unsuccessfully* that the Court's above language with reference to the Twenty-First Amendment, be modified to apply only to those situations in which the State itself operates the liquor business, i.e. monopoly states. The reason advanced being the basic anti-trust principles forwarded in that lawsuit. Both the post opinion letter and the Court's rejection are a matter of record in the *Midcal* Case.

Hence, designation of wholesalers and allocation of territories is directly responsive to structuring the liquor distribution system, as left to the states by the Twenty-First Amendment to the United States Constitution. The territorial arrangements under House Bill 2020 have led to an orderly marketing scheme and intense interbrand competition. In regard to this latter point, see the statistics of the Director of the Alcoholic Beverage Control Division, Kansas Department of Revenue at Appendix A which shows an increase of approximately ten thousand line items available for sale in the State of Kansas in the twelve-month period since the introduction of the franchise system to the state. Also, see Appendix B regarding wholesale and retail prices in Kansas under franchising as compared to open-wholesaling.

The state's interest in a distribution system which designates wholesalers and allocates territories is preserving a three-tier scheme which has been in existence in the alcoholic beverage industry for many years throughout the licensed states as a means of preventing abuse of a substance akin to abuse. In this regard see the outstanding work of F. Switzer, *The Three-Tier System of Distribution in the Wine and Spirits Industry*, W.S.W.A. (1975), regarding the three tier system of distribution, a part of the record before the trial court and the Supreme Court of the State of Kansas.

2. *The validity of H.B. 2020 should not be determined on the basis of the antitrust laws.*

Antitrust laws and specifically an analysis of the

"rule of reason" is an inappropriate test as to the constitutionality of a state statute; particularly when the statute in question has been upheld by the Kansas Supreme Court on other grounds as well.

That portion of H.B. 2020 which requires a supplier to appoint an exclusive distributor within a designated territory does not mandate a supplier to violate the law. This Court has acknowledged that vertical distribution schemes similar to H.B. 2020 are not facially violative of the antitrust laws. In *Continental T.V., Inc. vs. G.T.E. Sylvania, Inc.*, 388 U. S. 365, (1977) the court overruled its holding of *United States vs. Arnold, Schwinn and Co.*, 433 U. S. 36 (1977), that territorial confinement and customer allocation were illegal, *per se.* Thus, the instant case is not one where antitrust practices are regarded illegal, *per se,* without regard to the market power of the parties, the purpose of the restraint, or alleged good business reason for the practice. See *Northern Pacific Railroad vs. United States*, 356 U. S. 1 (1958). In the instant cause "rule of reason enforcement," which *Sylvania* substituted for *Schwinn's, per se* rule, taking a wide variety of factors into account, including market power, purpose and business practices, should be used in determining the illegality alleged. Under §1 of the Sherman Act, 15 U.S.C. §1, the applicable test to determine whether a restraint is unreasonable or not, is to be the "rule of reason."

Factual determinations under §1 of the Sherman Act can only be made pursuant to a full evidentiary hearing taking into account all the circumstances of the case. That

has not been done here. Business activities subjected to antitrust analysis and specifically the "rule of reason" test cannot be evaluated in this type of proceeding. *White Motor Company vs. United States*, 372 U. S. 253, 259, 263-64 (1963).

A rule of reason examination under the antitrust laws has, as best we can determine, never been used to invalidate a state law. Application of the rule of reason does not lend itself to summary adjudication. *White Motor Company vs. United States, Id.* at p. 259.

3. *Midcal inapplicable to case at bar.*

Midcal "presented a successful antitrust challenge to California's resale price maintenance and price posting statutes for the wholesale wine trade. The issue in this case [was] whether *those* state laws are shielded from the Sherrman Act by either the "state action" doctrine of *Parker v. Brown,* 317 U. S. 341 (1943) or §2 of the Twenty-First Amendment." *Midcal, Id.* at p. 97.

Wholesale prices as established by suppliers under "fair trade" doctrines are not at issue in *Colby*. Alleged operational impediments upon the Kansas marketplace was at issue.

In Kansas the State's involvement in all phases of each of the three-tiers of its distribution system is sufficient to establish antitrust immunities under *Parker*. Who better than the highest court of the state to determine that question? The distribution system is founded upon clearly

articulated and affirmatively expressed state policies, including temperance (although same was not true in *Midcal*). The state of Carey Nation is 46th in adult per capita consumption of distilled spirits of all the states, in this regard see Appendix C. Kansas distributes solely through package stores which may not offer other commodities nor may they promote their products. And by constitutional mandate "the open-saloon shall be and is hereby forever prohibited." Article 15, §10 Constitution of the State of Kansas. By a complex set of laws and regulations having the force and effect of law there is active supervision of supplier, distributor, and retailer practices and transactions. A complete evidentiary hearing which has *not* been conducted, would reveal, distinquishable from *Midcal*, that a pointed re-examination of the marketplace occurs, and such examination is by law a responsibility of state officials in order to preserve an orderly market free from the abuses akin to alcoholic liquors. In Kansas the system of promoting temperance and protecting the three-tier system is more substantial than the national policy of competition. That view could be supported by evidence, were it that such a fact finding process had occurred.

4. *Case at Bar Premature.*

Whether or not the designation of a distributor results in unreasonable restraint is factually premature and inappropriate in this type of proceeding. While the *Sylvania* majority opinion suggests that the court may in the future accept more rigorous, *per se* treatment for selected applications of territorial and customer restrictions, this is not the appropriate case for that finding in summary

fashion. The court stated in *Northern Pacific Railway Co. v. U. S.* 456 U. S. 1 (1958), that to make a departure from the "rule of reason" standard must be based upon demonstrable economic effects rather than--as in *Schwinn*--upon formalistic line drawing. *Sylvania, Id.* at pages 58-59.

This court has rejected the notion that a state law can be invalidated on the basis of assumed presumed or speculative facts. *Joseph E. Seagram & Sons, Inc. vs. Hofstetter*, 384 U. S. 35, 46 (1966). There is a strong policy against invalidating the state regulatory schemes in the absence of a clear showing of irreconcilable conflict with federal law. *Swift & Co. vs. Wickham*, 364 Fed. 2d 241, 246 (Second Circuit 1966) *cert. denied*, 385 U. S. 1036, 87 S.C. 776; 17 L. Edition 2nd 683 (1967).

In reality, appellant's main complaint is that they were not designated as distributor of products of their choice. It is the complaint of "disgruntled businessmen" as it was coined before the trial court. Appellants express no desire to necessarily return to "open wholesaling." It is that the appellants desire the right to choose and pick, which results in no less of a designation scheme. Exclusivity of territory and territorial allocations are secondary to the appellant's real concern.

5. "Open Wholesaling" vs. Designation of Distributors.

Kansas has gone through the transition from "open wholesaling" to the selection of exclusive distributors within a designated territory after numerous hours of

legislative contemplation and study. The open wholesaling concept led to a stagnation of interbrand competition. In this regard see again Appendix A showing the increase in brand line items (all items by size and brand). Open wholesaling of alcoholic beverages exists only in two other markets--Oklahoma and Minnesota. In Oklahoma the number of wholesalers has declined in recent years from twenty to six. It is self-evident that a franchise wholesaler will commit resources and manpower to develop and protect specific brands, which of marketing necessity will create interbrand competition. New brand owners and new brands entering the marketplace use designated distributors in order to induce competent and aggressive distributorships to make investments of capital and labor necessary in the distribution of new products. Also, established brand owners use designated distributors to induce distributors to engage in promotional activities or provide services necessary, as may be authorized under law, to the efficient marketing of their products. In this regard it is appropriate to acknowledge the redeeming virtues attributable to vertical restructions. Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his product. These redeeming virtues are implicit in every decision sustaining verticle restrictions under the rule of reason. *G.T.E. Sylvania, Inc., Id.* at 5455, states:

> "Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain

efficiencies in the distribution of his products. These 'redeeming virtues' are implicit in every decision sustaining vertical restrictions under the rule of reason. Economists have identified a number of ways in which manufacturers can use such restrictions to compete more effectively against other manufacturers. See, e.g., Preston, Restrictive Distribution Arrangements: Economic Analysis and Public Policy Standards, 30 Law & Contemp. Prob. 506, 511 (1965). For example, new manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer. Established manufacturers can use them to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products, such as automobiles and major household appliances. The availability and quality of such services affect a manufacturer's goodwill and the competitiveness of his product. Because of market imperfections such as the so-called 'free rider' effect, these services might not be provided by retailers in a purely competitive situation, despite the fact that each retailer's benefit would be greater if all provided the services than if none did." Posner, supra, n. 13., at 285; cf. P. Samuelson, Economics 506-507 (10th ed. 1976)."

6. *Affirmation Provisions under Kansas Law providing pointed re-examination of prices.*

There is no valid relationship between the selection of distributors under the amendments of the Kansas Liquor Control Act set forth in House Bill 2020 and the potential for higher resale prices to the consumer. Under the Kansas statutory provisions, as compared to California before *Midcal*, a supplier exercises little or no control over the ultimate price of his brands. House Bill 2020 contains the provision at §6 which was part of the preexisting law which states as follows:

> "That sales prices of alcoholic liquor sold by manufacturers and others to distributors licensed in this state should be no higher thatn the lowest price for which the same is sold by distributors anywhere in the Continental United State." (Now Kansas Statutes Annotated 1979 Supp. 41-4111 (a)).

That provision, commonly referred to as "affirmation," is intended to assure the residents of this state that the price of alcoholic beverages is at least as low as the same brand being sold within any other jurisdiction in the United States. Therefore, in the State of Kansas the price from the manufacturer to a distributor is totally dictated by State law designed to assure the lowest price possible. In view of affirmation, the testimony and conclusions reached by Dr. Terrell, as set forth on page 11 of the jurisdictional statement, relative to the premise of H.B.

2020 leading to higher consumer prices, is totally without merit. In particular, reference Appendix B prepared by the Kansas Wine and Spirits Wholesalers Association which demonstrates that wholesale prices in Kansas as compared with those of surrounding states are compatible or lower than those of its neighbor, as of one year after franchising became the law in Kansas. Effectively, the distributor designation provision of H.B. 2020, which appellants attack, has no influence over the pricing of alcoholic beverages in the State of Kansas. The structure of affirmation has been upheld by this court in *Joseph E. Seagrams and Sons, Inc. vs. Hofstetter*, 384 U. S. 35 (1966).

Also, certain of the statistical data in Appellant's statement is, we believe, misleading. The *Kansas City Star* article, "Law Hasn't Cut Kansas Liquor Cost" is referenced; but that article is not an extensive survey based on proper economic research. Further, the data at page 10 and in Appendix F are based on case shipments under "open-wholesaling" when Kansas only had one-third the line items (see Appendix A) available for retail sale. And Appendix F is misleading inasmuch as it implies that a given single firm has a share of the market place in those percentages as set forth in column one. Not true. Those figures, again based on the "open-wholesaling" system shipments, have applicability to different firms. For example, Firm A might have allegedly 90% of rum sales, but Firm B has 58.9% sales of cordials, and no listing is made to show that Firms C, D and E have in excess of 50% of wine sales. Wine comprises a significant share of market sales, and data relative thereto is not provided this Court. Were it not that Appellants have attempted to provide

data not in evidence below, we would likewise not have to do so to demonstrate the fragility of their position. The transformation from the concept of "open-wholesaling," which has existed only in three states and which resulted in the decline of the number of wholesalers, stagnation of brand promotion, minimal interbrand competition, resistance to the introduction of new brands, and a weakening of financial structures, was necessary *and was desired by the elected legislature.* In this regard see the report of the Interim Committee on Liquor Laws, a part of the record before the trial court. And there is ample authority, both legal and economic, to support the argument that designated distributors will commit more resources, manpower and active promotion which result in greater interbrand competition. This court endorsed such notion as quoted in *G.T.E. Sylvania, Inc. supra* at page 12. Further, the authority to choose the distributor is a more promising opportunity for the introduction of new brands. Appendixes B-1 and B-2 draw into question the econimic forcasts made at the trial court level as set forth at page 11 of Appellants' statement.

7. *State Supervision and Market Consentration.*

Appellants contend H.B. 2020 lacks state supervision. This contention is unjustified. Brand owners doing business in the State of Kansas must be authorized to enter this marketplace, must register brands, must comply with filing and recording procedures on a monthly basis, including verified statements that the price at which they are selling their products to Kansas distributors is as low as any other price being charged for the same product in the

Continental United States. Further regulations regarding the allocation and designation of territory have been promogated as authorized by the statute. Provided private parties engage in lawful activities, their conduct is at all times subject to private party antitrust actions or governmental actions pursuant to the antitrust laws both federal and state governments.

Appellants contend House Bill 2020 will result in market concentration by a few distributors. It is a reasonable expectation that whether a brand owner chooses a distributor or a distributor chooses its brands that certain wholesalers will attain greater success that others. There is nothing unique about the varying success of wholesalers in the alcoholic beverage industry or in any other industry. In fact, through a thorough fact finding inquiry into the wholesale liquor business throughout the United States there would be shown a reduction in the number of wholesalers. However, such cannot be proven without a full complete evidentiary proceeding at a trial court level under a properly brought antitrust cause of action. The fact that the wholesale liquor business becomes concentrated is more accurately the result of aggressive merchandising and management rather than being caused by unlawful activities. Further, this concentration is also a by-product of the strict statutory criteria governing those who may be licensed as distributors of alcoholic liquors in the State of Kansas. In this regard, see Kansas Statutes Annotated 41-311, which provides minimum residency requirements, absense of felony convictions and other such prohibitions, governing those who may be licensed.

CONCLUSION

Appellants urge this court to apply the doctrines of *Midcal* to the case at bar. Paradoxically--how is this court to apply a string of cases dealing with price resale maintenance provisions on the subject of the anti-trust validity of lawfully enacted and promulgated statutes pursuant to the Twenty-First Amendment of the Federal Constitution relating to vertical restrictions upon a system of distribution? The two subjects are not harmonious, the California factual circumstance and Kansas factual circumstance differ and thus the *Midcal* Case does not have direct applicability to the case at hand. In the words of appellants, the only question before the court on a Federal appeal basis is the validity under Federal anti-trust laws of the territorial exclusivity arrangements, governing a product which history has taught us must be supervised both in its trafficing and use.

The enacting of H.B. 2020 does not eliminate intra-brand competition inasmuch as different territories can be established in Kansas between suppliers and wholesalers, thus allowing territorial competition between brands. In fact, this occurs. There are price differentials for particular products between territories across the state. There is no restriction upon consumers or private clubs prohibiting them from purchasing only from licensed retailers in the same geographical territory in which they reside.

There is no absence of state supervision. If entrenchment of the wholesale market occurs (and it has not) it is not because of the enacting of H.B. 2020; rather, it is due

to the strict qualifying criteria which prevade the Liquor Control Act. The applicability of preceding years' percentages and case sales to alleged market share are inappropriate inasmuch as the brands for alcoholic liquor have drastically increased in the twelve (12) months since the effective date of the amended law.

The questions are not substantial inasmuch as the *Midcal* paradox of applicability does not require reversal of the Kansas Courts' Twenty-First Amendment ruling. The Kansas Supreme Court made its determination on reasons other than a federal question. House Bill 2020 is not invalid on its face under the federal anti-trust law; and, on the record presented there is insufficient evidence to make a determination of such invalidity.

There is much argument in the jurisdictional statement that is unsupported by the record. The introduction of new evidence which was not before the court at the time of trial, or the subsequent appeal, confirms that this case lacks a sufficient evidentiary basis upon which the court can make the determination appellants desire.

Thus, for the foregoing reasons a motion to dismiss is appropriate, and a motion to affirm is likewise appropriate.

Respectfully submitted,

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APPENDIX A

COMPARISON OF LINE ITEMS AVAILABLE FOR SALE IN KANSAS 1978-1979-1980

1. **Definitions:**

A. **"Alcoholic Liquor"**: Means alcohol, spirits, wine, beer, and every liquor or solid, patented or not, containing alcohol, spirits, wine or beer and capable of being consumed as a beverage by a human being, but shall not include any beer or cereal malt beverage containing not more than three and two-tenths percent (3.2%) alcohol by weight.

(1) **"Alcohol"** means the product of distillation of any fermented liquor, whether rectified or diluted, whatever the origin thereof, and includes synthetic ethyl alcohol but does not include denatured alcohol or wood alcohol.

(2) **"Spirits"** means any beverage which contains alcohol obtained by distillation, mixed with water or other substance in solution, and includes brandy, rum, whisky, gin or other spiritous liquors, and such liquors when rectified, blended or otherwise mixed with alcohol or other substances.

(3) **"Wine"** means any alcoholic beverage obtained by the normal alcoholic fermentation of the juice of sound, ripe grapes, fruits or berries, or other agricultural products, including such beverages containing added alcohol or spirits or containing sugar added for the purpose of correcting natural deficiencies.

(4) **"Beer"** when its meaning is not enlarged, modified, or limited by other words, means a beverage, containing more than three and two-tenths percent (3.2%) alcohol by weight, obtained by alcoholic fermentation of an infusion or concoction or barley, or other grain, malt and hops in water and includes beer, ale, stout, lager beer, porter and similar beverages having such alcoholic content. NOTE: Beer is not included as a line item in this report.

B. Line Item: Line item is a brand item (container) of alcoholic liquor offered for sale in the Kansas market. Line items are considered from the following viewpoint:

(1) From the Supplier point-of-view, a line item is a brand item (container) of alcoholic liquor, authorized for sale in Kansas, posted by the supplier, available to the wholesaler franchisee, for sale to the retail licensee.

(2) From the Wholesaler (Franchisee) point-of-view, a line item is a brand item (container) of alcoholic liquor, authorized for sale in Kansas, posted by the supplier, posted by the wholesaler, and is offered for sale to the retail licensee.

2. Line Items available in the State of Kansas on July 1, 1978, 1979 and 1980 were:

1978

Total Line Items: 3,964

1979

Total Line Items: 4,366

1980

Total Line Items: 14,883

3. Total number of Spirits and Wine Suppliers furnishing the above Line Items:

YEAR	SPIRIT AND WINE SUPPLIERS
1978	93
1979	99
1980	169

Source: Office of the Director of Alcoholic Beverage Control; Kansas Department of Revenue

APPENDIX B-1

COMPARISON OF CONSUMER PRICES FOR BETTER SELLING BRANDS OF WINE & CHAMPAGNE

SEPTEMBER 1979 AND 1980

OPEN WHOLESALING

	Size	September 1979	September 1980 (Note 2)	September 1980 (Franchise)
Gallo (Chablis Blanc, Hearty Burgundy, Burgundy, Rhine, Pink Chablis, Red Rose)	3.0	$ 6.87	$ 7.54	$ 6.99
	1.5	3.99	4.62	3.99
T. J. Swann	750	1.90	2.10	1.91
Inglenook Navalle (Burgundy Chablis, Rhine, Vin Rose)	1.5	4.22	5.05	4.20
Manischewitz Cream Red & White Concord	750	3.31	3.69	2.80
Paul Masson (Burgundy, Chablis, Rhine, Rose)	3.0	8.12	8.81	7.99
	1.5	4.75	5.16	4.98
Almaden Mtn Wines (Red Burgundy, Chablis, Red Claret, Vin Rose, Rhine, Sauterne)	3.0	7.25	8.36	7.09
	1.5	4.34	5.14	4.15

OPEN WHOLESALING

	Size	September 1979	September 1980 (Note 2)	September 1980 (Franchise)
Mogen David Concord	1.5	4.89	5.20	5.08
Taylor Lake Country Wines	1.5	5.42	5.71	4.49
Blue Nun Liebfraumilch	750	5.80	6.07	5.49
Cella Lambrusco	750	3.10	3.69	2.99
Mateus Rose	750	4.94	4.79	4.89
Yago Sant'Gria	750	3.45	3.57	2.99
Riunite Lambrusco	750	3.13	3.29	3.09
Jacques Bonet Champagne	750	3.10	3.44	3.29
Andre Champagne	750	3.10	3.44	3.09
Totals		$81.68	$89.67	$79.50
Percent Increase (Decrease) Over Sept. 1979			9.78%	(2.67%)

Notes:

(1) The above brands of wine & champagne accounted for 540,420 cases or 76% of the wine and champagne shipped into Kansas in 1979

(2) Adjusted for increased freight charges and supplier price increases in the past 12 months

COMPARISON OF CONSUMER PRICES FOR BETTER SELLING BRANDS OF SPIRITS

SEPTEMBER 1979 AND 1980

	1.0 LITER SIZE OPEN WHOLESALING			750 ML SIZE OPEN WHOLESALING		
	September 1979	September 1980 (Note 2)	September 1980 (Franchise)	September 1979	September 1980 (Note 2)	September 1980 (Franchise)
Old Charter, 8 Year	$ 9.27	$ 9.59	9.49	7.14	7.42	7.39
Ancient Age	7.76	8.02	7.50	6.11	6.33	5.90
Jim Beam	7.41	7.37	7.29	5.76	5.63	5.75
Old Taylor	8.32	8.51	8.36	6.35	6.56	6.49
Jack Daniels Black	11.27	11.72	11.94	8.64	8.95	9.12
Ten High	6.67	6.57	6.33	5.14	5.47	5.54
Wellers	9.22	9.77	8.99	7.12	7.56	7.48
Mattingly & Moore	6.08	6.70	5.79	4.85	5.34	4.79
Seagrams 7 Crown	8.09	8.32	8.38	6.11	6.30	6.39
J & B Scotch	12.41	14.00	12.98	9.55	10.75	9.99
Cattos Gold	6.92	8.10	6.98	5.61	6.31	5.99
J. W. Dant Scotch	8.12	8.52	7.99	6.20	6.46	6.55
Cutty Sark	12.23	14.01	12.89	9.08	10.48	9.49
Canadian Mist	7.81	8.16	8.49	5.99	6.31	6.49
Canadian Club	10.61	10.66	10.59	8.01	8.06	8.23
Seagram's V. O.	10.60	10.67	10.59	8.01	8.07	7.98
Popov 80 Vodka	5.50	5.95	5.39	4.35	4.64	4.39
McCormick 80 Vodka	5.69	5.77	5.49	4.46	4.58	4.67
Smirnoff 80 Vodka	7.34	7.82	7.79	5.61	5.97	5.99

	1.0 LITER SIZE OPEN WHOLESALING			750 ML SIZE OPEN WHOLESALING		
	September 1979	September 1980 (Note 2)	September 1980 (Franchise)	September 1979	September 1980 (Note 2)	September 1980 (Franchise)
Beefeater Gin	10.98	12.80	11.99	8.49	10.48	9.28
Seagram's Gin	7.32	7.38	7.29	5.54	5.61	5.68
Gilbey's Gin	6.94	6.83	6.70	5.27	5.34	5.25
Bacardi Rum	7.36	7.84	7.79	5.83	6.21	5.99
Castillo Rum	6.19	6.39	5.99	4.82	4.97	3.99
Jose Cuervo White Tequila	8.53	9.40	9.39	6.70	7.28	7.29
Don Emilio Tequila	6.41	6.28	5.20	4.95	5.25	3.90
Kahlua Coffee Liqueur	14.82	15.39	15.19	10.27	11.72	11.96
TOTALS	$229.87	$242.54	$232.79	$175.96	$188.05	$181.96
Percent Increase Over September 1979	-	5.51%	1.27%	-	6.87%	3.41%

Notes:

(1) Above spirit brands accounted for 661,751 cases or 52% of the spirit shipments into Kansas in 1979

(2) Adjusted for increased freight charges and supplier price increases in the past 12 months

Source: Kansas Wine and Spirits Wholesaler Association

APPENDIX B-2

COMPARISON OF WHOLESALER PRICES TO RETAILER IN KANSAS AND MISSOURI JULY 1980

Source: Kansas and Missouri Wholesaler Price Books for July 1980; Kansas Wine and Spirits Wholesalers Assn.

Item-Bourbon	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
Old Charter 10 yr.	1.75	Standard	$ 87.30	$ 84.50	$14.70	$14.58
Old Charter 10 yr.	7.50	Standard	78.00	75.95	6.60	6.60
Old Charter 8 yr.	1.75	Standard	72.36	66.99*	12.21	11.67*
Old Charter 8 yr.	7.50	Standard	67.80	63.50*	5.75	5.50*
Old Charter 8 yr.	2.00	*Item is 7 yr. old	83.84	81.49*	1.78	1.76*
Old Forrester 86°	1.75	Standard	66.72	64.99	11.27	11.34
Old Forrester 86°	7.50	Standard	63.96	64.99	5.43	5.67
Old Forrester 86°	2.00	Standard	79.20	76.99	1.70	1.67
Early Times	1.75	Standard	57.36	62.99	9.71	11.00
Early Times	1.L	Standard	71.52	73.49	6.06	6.37
Early Times	7.50	Standard	50.04	57.49	4.27	5.04
Early Times	5.00	Standard	78.00	79.99	3.33	3.46
Early Times	2.00	Standard	68.16	69.99	1.47	1.52
Ezra Brooks 7 yr.	1.75	Famous	65.34	66.99	11.04	11.67
Ezra Brooks 7 yr.	Qts.	Famous	71.52	69.99	6.06	6.08
Ezra Brooks 7 yr.	7.50	Famous	57.48	57.99	4.89	5.08
Ezra Brooks 7 yr.	Pts.	Famous	74.40	73.99	3.18	3.21

Item-Bourbon	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
Cabin Still	1.75	Famous	$ 59.28	$ 52.99	$10.03	$ 9.33
Cabin Still	1.L	Famous	65.88	59.99	5.59	5.25
Cabin Still	7.50	Famous	53.76	49.99	4.58	4.42
Cabin Still	Pt.	Famous	70.56	64.99	3.02	2.83
Cabin Still	2.00	Famous	68.16	64.99	1.47	1.41
W. L. Waller	1.75	Famous	71.40	73.99	12.05	12.83
W. L. Waller	1.L	Famous	82.68	85.99	6.99	7.42
W. L. Waller	7.50	Famous	65.88	66.99	5.59	5.83
W. L. Waller	5.00	Famous	83.76	87.99	3.57	3.76
W. L. Waller	2.00	Famous	83.04	81.99	1.78	1.76
Jim Beam 4 yr. 80°	1.75	Standard	57.84	55.50	9.79	9.65
Jim Beam 4 yr. 80°	7.50	Standard	52.44	54.99	4.47	4.54
Jim Beam 4 yr. 80°	5.00	Standard	68.88	67.40	2.95	2.99
Jim Beam 4 yr. 80°	2.00	Standard	64.32	64.99	1.39	1.35
Item-Scotch						
Dewars White Label Scotch	1.75	Sunflower	93.30	104.99	15.55	18.00
Dewars White Label Scotch	7.50	Sunflower	93.24	98.99	7.77	8.25
Dewars White Label Scotch	10th	Sunflower	102.96	99.99	4.37	4.29
Dewars White Label Scotch	2.00	Sunflower	119.52	123.99	2.56	2.65
Haig Pinch Scotch	1.75	Sunflower	151.26	158.99	25.36	27.00
Haig Pinch Scotch	7.50	Sunflower	129.36	No Price	10.88	No Price
Haig Pinch Scotch	10th	Sunflower	139.68	147.99	5.90	6.29

Item-Scotch	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
J & B Scotch	Gal.	Standard	100.35	**91.99**	33.45	**31.67**
J & B Scotch	1.75	Standard	**106.44**	106.99	**17.89**	18.33
J & B Scotch	Qts.	Standard	**110.76**	118.99	**9.33**	10.17
J & B Scotch	7.50	Standard	**92.04**	98.99	**7.77**	8.50
J & B Scotch	2.00	Standard	**120.48**	123.99	**2.56**	2.65
J. Walker Black Scotch	1.75	Famous	**$141.18**	$152.99	**$23.68**	$25.99
J. Walker Black Scotch	1.L	Famous	**171.36**	171.99	14.38	**13.99**
J. Walker Black Scotch	7.50	Famous	134.04	**133.99**	**11.27**	11.42
J. Walker Black Scotch	10th	Famous	**135.98**	145.99	**5.75**	6.18
J. Walker Black Scotch	2.00	Famous	165.12	**163.99**	3.49	**3.48**
J. Walker Red Scotch	Gal.	Famous	**97.23**	103.39	**32.71**	36.17
J. Walker Red Scotch	1.75	Famous	**103.62**	104.99	**17.42**	18.00
J. Walker Red Scotch	Qt.	Famous	**110.76**	113.99	**9.33**	9.75
J. Walker Red Scotch	7.50	Famous	**92.04**	98.99	**7.77**	8.50
J. Walker Red Scotch	10th	Famous	**91.20**	99.99	**3.88**	4.30
J. Walker Red Scotch	2.00	Famous	121.09	**109.99**	2.55	**2.40**
Chivas Regal	Gal.	Standard	**162.48**	171.26	**54.46**	58.09
Chivas Regal	1.75	Standard	**153.12**	154.55	**25.67**	26.23
Chivas Regal	7.50	Standard	135.00	**134.55**	**11.35**	11.47
Chivas Regal	10th	Standard	**141.60**	144.75	**5.98**	6.16
Chivas Regal	2.00	Standard	165.12	**164.99**	**3.49**	3.50
Inverhouse Scotch	1.L	Famous	**63.96**	71.99	**5.43**	6.25
Inverhouse Scotch	7.50	Famous	**51.00**	54.99	**4.35**	4.78
Inverhouse Scotch	10th	Famous	61.20	**56.99**	2.63	**2.47**
Inverhouse Scotch	2.00	Famous	64.32	**63.99**	**1.39**	1.41

Item-Gin	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
Beefeater Gin	Gal.	Standard	$116.70	$102.75	$38.90	$35.14
Beefeater Gin	1.75	Standard	92.40	92.30	15.55	15.84
Beefeater Gin	Qts.	Standard	99.48	101.99	8.39	8.75
Beefeater Gin	7.50	Standard	85.44	83.80	7.22	7.24
Beefeater Gin	2.00	Standard	105.12	103.95	2.24	2.26
Tanquerary Gin	1.75	Famous	92.40	88.69	15.55	15.88
Tanquerary Gin	Qts.	Famous	98.64	98.98	8.32	8.66
Tanquerary Gin	7.50	Famous	85.44	81.34	7.22	7.16
Tanquerary Gin	Pts.	Famous	102.48	101.43	4.35	4.44
Tanquerary Gin	2.00	Famous	105.12	99.47	2.24	2.17
Gordens Gin	1.75	Sunflower	57.84	56.85	9.79	10.17
Gordens Gin	1.L	Sunflower	65.76	63.70	5.58	5.67
Gordens Gin	7.50	Sunflower	50.16	49.99	4.27	4.50
Gordens Gin	5.00	Sunflower	66.72	64.68	2.86	2.87
Gordens Gin	2.00	Sunflower	63.36	63.70	1.39	1.42
Gordens Vodka	1.75	Sunflower	48.00	45.05	8.15	8.17
Gordens Vodka	1.L	Sunflower	52.80	49.00	4.50	4.42
Gordens Vodka	7.50	Sunflower	42.48	40.57	3.64	3.70
Gordens Vodka	2.00	Sunflower	51.84	49.99	1.15	1.10
Kahlua Coffee Liq.	1.75	Sunflower	117.72	119.79	19.77	19.95
Kahlua Coffee Liq.	1.L	Sunflower	136.68	138.99	11.49	12.04
Kahlua Coffee Liq.	2.00	Sunflower	119.04	125.99	2.55	2.63
Canadian Mist	1.75	Standard	60.36	64.99	10.57	11.33
Canadian Mist	1.L	Standard	72.48	74.95	6.14	6.48
Canadian Mist	7.50	Standard	54.72	56.99	4.66	4.99
Canadian Mist	5.00	Standard	78.00	77.95	3.33	3.37
Canadian Mist	2.00	Standard	68.16	69.95	1.47	1.52

Item-Brandy	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
E. & J. Brandy	1.75	Sunflower	$ 61.56	$ 61.49	$10.41	$10.75
E. & J. Brandy	1.L	Sunflower	**71.52**	72.49	**6.06**	6.29
E. & J. Brandy	7.50	Sunflower	**57.36**	58.49	**4.88**	5.12
E. & J. Brandy	5.00	Sunflower	**78.00**	79.99	**3.33**	3.46
E. & J. Brandy	2.00	Sunflower	**70.56**	71.99	**1.54**	1.56
Almaden Brandy	1.75	Famous	58.32	**54.99**	9.87	**9.57**
Almaden Brandy	Qts.	Famous	61.20	**59.99**	**5.20**	**5.20**
Almaden Brandy	10th	Famous	53.76	**52.99**	2.32	**2.31**
Paul Masson Brandy	1.75	Standard	63.00	**62.99**	**10.65**	11.00
Paul Masson Brandy	7.50	Standard	**57.48**	57.99	**4.89**	5.10
Paul Masson Brandy	2.00	Standard	**60.96**	71.99	**1.27**	1.55
CONCLUSIONS		Case Mo. Lower	49	Bottles Mo. Lower		27
Number of Spirits Items Compared: 101		Cases Kan's Lower	52	Bottles Kan's Lower		74
Bold Face = lower price			101			101
Item-Wine						
Paul Masson	1.5	Standard	**19.62**	22.45	**3.42**	4.25
Gamay Rose-Reisling French Colombard	7.50	Standard	**22.56**	26.95	**1.98**	2.50
Paul Masson Barbara	1.5	Standard	**16.02**	22.45	**2.67**	4.25
Paul Masson Barbara	7.50	Standard	**22.56**	26.95	**1.98**	2.50

Item-Wine	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
Paul Masson	1.5	Standard	$ 15.00	$ 22.45	$ 2.50	$ 4.25
Ruby Cabernet	7.50	Standard	22.56	26.95	1.98	2.50
Paul Masson						
Cabernet Sauvignon	7.50	Standard	39.12	41.95	3.39	3.70
Pinot Noir	7.50	Standard	35.04	36.95	3.02	3.30
Pinot Blanc	7.50	Standard	35.04	36.95	3.02	3.30
Pinot Chardonney	7.50	Standard	44.04	44.95	3.77	3.95
Pinot Chardonney	3.75	Standard	47.28	50.95	2.05	2.25
Paul Masson Carafes						
Burgundy-Rose-Chablis	1.L	Standard	27.48	31.50	2.39	2.88
Paul Masson Sparkling						
Champagne Brut Extra Dry	1.5	Standard	52.62	53.99	8.92	9.50
Pink-Cold Duck	7.50	Standard	52.32	53.99	4.46	4.75
Sparkling Burgundy	3.75	Standard	46.08	59.50	1.92	2.60
Almaden Mountain Wines	4.L	Famous	20.76	26.49	5.49	7.22
Red Burgundy-Red Claret	3.L	Famous	18.28	22.49	4.87	6.22
Rhine-White-Chablis	1.5	Famous	16.20	20.99	2.85	3.90
White Sauterne-Nectar Rose	7.50	Famous	20.16	23.99	1.78	2.20
Red Claret	3.75	Famous	27.60	26.49	1.23	1.20
Almaden Classic Varitals	7.50	Famous	33.84	39.49	2.92	3.49
Cabernet Sauvignon	3.75	Famous	40.80	42.49	1.78	1.87
Johannisberg Reisling	7.50	Famous	34.08	39.49	2.94	3.49
Pinot Noir-Pinot Chardonnay	3.75	Famous	40.56	42.49	1.77	1.87

Item-Wine	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
Almaden Sparkling Wines						
Brut Extra Dry,	7.50	Famous	$ 51.96	$ 56.49	$ 4.43	$ 4.99
Pink Sparkling Burg.	3.75	Famous	55.44	59.99	2.39	2.59
Blanc de Blanc	7.50	Famous	60.48	65.99	5.14	5.79
Gallo Table Wines	3.L	Sunflower	18.84	19.29	5.01	5.57
Hearty Burg.-Chablis Blanc	1.5	Sunflower	15.54	17.15	2.74	3.30
Rhine-Red Rose	7.50	Sunflower	17.64	19.50	1.57	1.87
Gallo Mountain Wines	3.L	Sunflower	16.36	19.29	4.39	5.57
Vin Rose-Rhinegarten	1.5	Sunflower	14.70	17.50	2.60	3.42
Chianti	7.50	Sunflower	15.96	19.50	1.43	1.87
Gallo Dessert Wines						
Livingston Creme Sherry,	1.5	Sunflower	16.74	16.29	2.94	3.24
Tawny Port, Very Dry Sherry	7.50	Sunflower	17.64	16.59	1.57	1.62
Gallo Dessert Wines	3.L	Sunflower	19.36	No Price	5.14	No Price
White Port-Sherry-Muscatel	1.5	Sunflower	15.54	15.69	2.74	3.11
Port-Cream Sherry	7.50	Sunflower	15.96	15.99	1.43	1.58
C.P.O. Sherry	3.75	Sunflower	17.52	15.99	.81	No Price
Gallo Varietal Wines						
Barbara	1.50	Sunflower	16.86	18.85	2.94	3.64
Barbara	7.50	Sunflower	17.64	21.49	1.57	2.04
Rose-Chenin Blanc	1.50	Sunflower	18.42	18.99	3.22	3.64
French Colombard	7.50	Sunflower	20.16	21.49	1.78	2.04
Sauvignon Blanc	1.50	Sunflower	20.46	20.29	3.56	3.88
Sauvignon Blanc	7.50	Sunflower	22.56	23.39	1.98	2.20

Item-Wine	Size	Kansas Company	Kansas Case Price	Missouri Case Price	Kansas Bottle Price to Retailer	Missouri Bottle Price to Retailer
Andre Champagnes-Dry-Cold Duck-Pink-Sparkling Burg.	7.50	Sunflower	$ 24.00	$ 23.69	$ 2.26	$ 2.24
Reunite Wines White-Rose-Red	1.5	Sunflower	24.60	25.25	4.25	4.66
	7.50	Sunflower	25.92	26.99	2.26	2.50
Bell Agio	1.5	Sunflower	24.00	21.99	4.11	4.07
	7.50	Sunflower	25.08	23.52	2.19	2.22

CONCLUSIONS
Number of Wine Items Compared: 50
Bold Face = lower price

Case Prices Missouri Lower	8	Bottle Prices Missouri Lower	3
Case Prices Kansas Lower	42	Bottle Prices Kansas Lower	46
	50		49*

*Mo. did not post bottle price on 3.75M size Gallo Dessert Wines

APPENDIX C

1. Adult per capita, based on legal drrinking age, consumption (Wine gallons). Extracted from The Liquor Handbook, A Gavin-Jobson Publication 1980.

States in Order of Ranking 1979	Adult Per Capita Consumption (Wine Gallons) 1979	1978
1. Nevada	9.65	10.87
11. Colorado	3.63	4.29
36. Nebraska	2.45	2.50
40. Missouri	2.28	2.34
45. Oklahoma	2.09	2.42
46. Kansas	2.09	1.93
51. Arkansas	1.67	2.12
Total U. S.	2.99	3.01

2. Apparent consumption of Distilled Spirits in Wine Gallons, 1975-1979: Extracted from Distilled Spirits Council of the U. S. Inc. publication 1975-1979:

	1975	1976	1977	1978	1979
Kansas	1.29	1.27	1.25	1.27	1.39
Nebraska	1.76	1.76	1.73	1.71	1.70
Colorado	2.49	2.48	2.32	2.71	2.47
Missouri	1.61	1.48	1.46	1.54	1.52
Oklahoma	1.54	1.41	1.62	1.61	1.62
Nevada	6.92	7.11	7.21	6.92	6.25
Arkansas	1.12	1.20	1.18	1.38	1.09
Total License States	2.13	2.13	2.14	2.18	2.17
Total Control States	1.64	1.65	1.66	1.69	1.70
Grand Total	1.98	1.98	1.99	2.03	2.03

No. 80-189

Supreme Court, U. S.
FILED
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MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

October Term, 1980

GRANT-BILLINGSLEY WHOLESALE LIQUOR CO., INC.,

Appellant,

v.

MICHAEL C. LENNEN, SECRETARY OF REVENUE FOR THE STATE OF KANSAS, *et al.*,

Appellees.

On Appeal from the Supreme Court of the State of Kansas

MOTION TO DISMISS OR AFFIRM BY APPELLEE STANDARD LIQUOR CORPORATION

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No. 80-189

IN THE

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GRANT-BILLINGSLEY WHOLESALE LIQUOR CO., INC.,

Appellant,

v.

MICHAEL C. LENNEN, SECRETARY OF REVENUE FOR THE STATE OF KANSAS, *et al.*,

Appellees.

On Appeal from the Supreme Court of the State of Kansas

MOTION TO DISMISS OR AFFIRM BY APPELLEE STANDARD LIQUOR CORPORATION

On the ground that the federal questions presented are so insubstantial as not to warrant further briefing or argument, appellee Standard Liquor Corporation ("Standard"), a licensed Kansas wine and spirits wholesaler and party-intervenor below, moves pursuant to Rule 16 for dismissal of this appeal or affirmance of the judgment of the Supreme Court of the State of Kansas, which sustained the constitutionality of newly enacted provisions of the Kansas liquor laws mandating exclusive territorial franchises challenged as violating the Sherman Act and, therefore, as repugnant to the Commerce and Supremacy Clauses of the federal Constitution.

Statement of the Case

This appeal is taken from the decision of the Kansas Supreme Court in *Colby Distributing Co., Inc.* v. *Lennen,* 227 Kan. 2d 179, 606 P.2d 102 (1980).[1] Finding unpersuasive a variety of claims that the new provisions were contrary to both state and federal constitutional requirements, the state court upheld the validity of the 1979 changes made in the Kansas structure for regulating alcoholic beverages[2] by Kansas House Bill No. 2020 ("H.B. 2020").

Both before and since the enactment of H.B. 2020, distillers, importers, vintners and other suppliers ("suppliers"), who are permitted in keeping with the so-called "three tier" system to sell only to licensed wholesalers, have been required to post their prices with the Department of Revenue's Division of Alcoholic Beverage Control ("ABC") and to affirm that the price of any brand and size sold to a Kansas wholesaler is as low as the lowest price charged elsewhere by that supplier.[3] Prior to H.B. 2020, the ABC Board of Review established a mandatory minimum markup percentage below which the wholesaler could not resell to the retailer. That markup was set at a level to cover all costs of doing business and to insure a profit to the wholesalers on each of the items they sold. (4a, 53a-56a) The minimum wholesaler-to-retailer price of

1. That opinion is Appendix A to appellant's Jurisdictional Statement. References to that and other appendices thereto will be by page number (*e.g.,* "4a"). References to "E——-" are to pages of the Report of the Special Committee on Liquor Laws appointed by the Kansas Legislature, which was Exhibit 4 in the trial record below and which is reprinted as an appendix hereto. References to "JS ——" are to pages of the Jurisdictional Statement.

2. See Kansas Liquor Control Act, Kan. Stat. Ann. §§41-101, *et seq.*

3. This price affirmation requirement is essentially identical to that which this Court upheld in *Joseph E. Seagram & Sons, Inc.* v. *Hostetter,* 384 U.S. 35 (1966).

every item, therefore, was fixed at a uniform level statewide. The minimum markup mandated was 15.5% on spirits and 26.5% on wines. (E4)

Under the so-called "open wholesaling" requirement of the prior regulatory structure, if a supplier elected to sell a brand to any Kansas wholesaler he also had to sell to any other distributor choosing to buy it. While no wholesaler was required to handle all brands purchased by any or all others, on those leading brands for which demand was greatest there was wasteful duplication of inventory, increased transportation expense because of smaller shipments to each wholesaler, and other higher costs to wholesalers, with resulting higher prices to consumers. (E4-E6)

During 1978, a Special Committee on Liquor Laws, set up by the Kansas Legislature, conducted hearings and consulted with the ABC concerning the "open wholesaling" requirement and the state-fixing of mandated minimum markups. The Committee heard testimony, *inter alia,* that these practices in combination forced distributors to carry nearly identical inventories, restricted competition to rivalry only on the basis of delivery service but with no promotion of individual brands, rewarded economic inefficiencies, guaranteed a profit to wholesalers, raised costs and resulted in higher prices to consumers. Because consumer prices for alcoholic beverages in neighboring states were lower than in Kansas, the Committee reported that an estimated $17 million worth of liquor was illegally purchased in 1977 by Kansans from out-of-state sources, with a resulting tax loss to the state of more than $2 million. (E3-E7)

The Committee recommended elimination of price controls at the wholesaler level and replacement of the "open wholesaling" system by exclusive territorial franchises. Under that proposal, a single wholesaler in a specified territory would represent each particular brand and re-

tailers located in that territory could buy that brand only from that franchised wholesaler. The Committee concluded that the proposed franchise system would eliminate many of the economic inefficiencies fostered under the "open" structure, would reduce the costs attributable to duplicative inventories, would bring about a more efficient distribution system, would introduce competition into the wholesale liquor industry, and would result in more equitable, lower prices for consumers. (E5-E7)

H.B. 2020 followed the Committee's study and recommendations. (5a) First, it removed the old price controls at the wholesale level. Wholesaler prices to retailers are now to be determined independently by each franchised distributor in competition with the brands of others. As the Kansas Supreme Court concluded, by thus "allowing the liquor price to seek its own level at the second tier of the liquor system, the legislature has released liquor pricing from its former status as a totally controlled commodity." (19a)

Second, no wholesaler is to sell a brand unless there is filed with the ABC a written agreement with the supplier specifying the territory within which the wholesaler is to sell that brand to retailers. No supplier is to "grant a franchise for the distribution of a brand to more than one distributor for all or part of any designated territory." (46a)

Third, with a single wholesaler thus accountable for representing a brand, broad obligations are imposed upon that franchised wholesaler to serve all retail accounts in his territory and to do so on a non-discriminatory basis with respect to both price and the supporting services which promote sale of the brand. If he fails to provide such service and pricing, the statute requires that the ABC director "shall revoke the license of such distributor." Further, in the event of any supply shortage which pre-

vents filling the orders of all retailers, apportionment plans must be approved by the director. (52a-53a)

Following enactment of H.B. 2020, three wholesalers (including appellant), dissatisfied with the brand franchises they had negotiated in the separate local markets which they served, sought a declaratory judgment and injunction in the Kansas District Court against enforcement of various provisions of the new legislation. On August 6 and 7, 1979, evidence and argument both *pro* and *con* were offered at a trial. Because Section 11 of H.B. 2020 (57a) provided a 120-day transition period and because the district court had temporarily enjoined enforcement of the new provisions, no evidence of their actual operation and effects was introduced and the trial court made no findings as to such issues of fact. Instead, without citation of judicial precedent, that court concluded on the face of the statute that its requirement of exclusive territorial franchises violated the Sherman Act.[4] (24a-39a)

The Supreme Court of Kansas stayed the trial court's determination pending appeal. In deciding the matter thereafter, the state supreme court addressed itself to the constitutionality of the new legislation primarily "on its face", because "the provisions of H.B. 2020 were not in effect on the date of trial, [thus] rendering the evidence presented highly speculative." (14a) Reversing the trial court's determination of the franchise issue, the appellate court concluded that the new provisions were a proper exercise of the state's regulatory power over liquor under the Twenty-first Amendment.

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4. The trial court also accepted the plaintiffs' argument that minimum markup percentages to be established by the ABC at the retailer-to-consumer level constituted an unlawful delegation of price-fixing authority to the wholesalers. That determination was reversed by the Kansas Supreme Court, and appellant apparently does not here appeal from that part of the decision below.

Further, however, as a separate and independent basis for upholding the provisions of H.B. 2020, the Kansas Supreme Court also found that on their face those provisions withstood the allegations of Sherman Act violation. Recognizing that "H.B. 2020 is an attempt to obtain liquor prices which are competitive with surrounding states by introducing competition into the three-tiered structure [of alcoholic beverage distribution]" and that at the distributor level H.B. 2020 "allows the price to seek its own level in the market place as a result of competition between brands" (5a), the Kansas Supreme Court concluded:

> "By allowing the liquor price to seek its own level at the second tier of the liquor system, the legislature has released liquor pricing from its former status as a totally controlled commodity. The price is no longer totally regulated, totally fixed and can now fluctuate as the competition in the market place will determine. With respect to exclusive franchising, we have noted there are now at least two distributors operating in every area of the state. Each distributes different brands, which compete with one another. Although each distributor completely controls the distribution of its brands within its territory, we find the competition among brands to be sufficient to withstand claims of restraint of trade. . . .
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> ". . . The stated legislative purpose is to introduce competition into the pricing of liquor to the public, thereby promoting the public welfare and stopping illegal liquor traffic from out of state by offering a more competitive price. There is nothing before us to show the stated purpose is not working. . . ." (19a-20a)

ARGUMENT

Appellant contends that this Court's decision in *California Retail Liquor Dealers Ass'n.* v. *Midcal Aluminum, Inc.*, —— U.S. ——, 100 S. Ct. 937 (1980), requires reversal (1) because the Kansas Supreme Court purportedly ruled that the Twenty-first Amendment permits Kansas to enact liquor legislation wholly unfettered by the Commerce Clause and federal antitrust legislation and (2) because H.B. 2020 allegedly violates the Sherman Act.

A. There Is No Showing That H.B. 2020 Conflicts With the Sherman Act.

1. Unlike the vertical price-fixing in per se violation of the Sherman Act found in Midcal, *the exclusive territorial franchises mandated by H.B. 2020 require full rule-of-reason analysis.*

To invalidate state legislation on such federal grounds, patently it must be shown at the outset that the state law is preempted because it mandates or attempts to authorize private conduct which would violate the antitrust laws and is, therefore, invalid under the Supremacy Clause.[5] That conclusion has been most recently confirmed by this Court's analysis in the *Midcal* case ("The threshold question is whether California's plan for wine pricing violates the Sherman Act"). (100 S.Ct. at 941)

Any claim that *Midcal* is controlling here as to that threshold issue must rest on a wholly superficial comparison of the two cases. In *Midcal*, this Court upheld a line of California state court decisions striking down that state's statutory delegation to private parties of the unsupervised power to set minimum resale prices to be

5. *See, e.g., Joseph E. Seagram & Sons, Inc.* v. *Hostetter*, 384 U.S. 35, 41 (1966); Note, "*Parker* v. *Brown* Revisited," 77 Col. L. Rev. 898, 899 n.7 (1977).

charged by the purchasers of their brands.[6] Such vertical price-fixing, lacking even the pretense of state review or involvement, constituted a *per se* violation of the Sherman Act on the face of the statutes and without more.

To find a state statute repugnant to the antitrust laws, *Midcal* and the California decisions it endorsed require that there must be a *per se* violation or at least, as the California Supreme Court declared, "a clear violation of the Sherman Act" mandated by the state.[7] Neither *Midcal* nor the California precedents involved state regulation of liquor distribution structure and the accountability of an exclusive distributor within a specified territory for non-discriminatory, equal access servicing of all retail accounts, regardless of their volume, distance from his warehouse, or marginal profitability owing to the high cost of serving them.

In sharp contrast, the legislation challenged here involves non-price vertical arrangements which require a full "rule-of-reason" analysis. This Court, by overruling the *per se* holding of *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), unequivocally re-established the proposition that vertical non-price restrictions, including exclusive territorial confinement of a distributor by a supplier, even when effected solely by private parties, require a rule-of-reason evaluation because they fail to meet the "demanding standards" for invoking the *per se* rules.[8]

6. See *Rice* v. *Alcoholic Beverage Control Appeals Board*, 21 Cal. 3d 431, 146 Cal. Rptr. 585, 579 P.2d 476 (1978); *Capiscean Corp.* v. *Alcoholic Beverage Control Appeals Board*, 87 Cal. App.3d 996, 151 Cal. Reptr. 492 (1979); *Midcal Aluminum, Inc.* v. *Rice*, 90 Cal. App. 3d 979, 153 Cal. Rptr. 757 (1979).

7. See *Rice, supra*, n.6, 579 P.2d at 482.

8. *See Northern Pacific R. Co.* v. *United States*, 356 U.S. 1, 5 (1958) ("there are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use").

Continental T.V., Inc. v. *GTE Sylvania, Inc.*, 433 U.S. 36, 50 (1977). Here there has been neither opportunity nor effort in the proceedings below to assess actual competitive experience or the market effects of the franchise system at issue, particularly considering the state mandated requirement that the franchised wholesalers supply and service all retailers in their territories without discrimination in price or other competitive benefits and through rationing if necessary.

Appellant pays only grudging lip service to this Court's *Sylvania* decision, mistakenly characterizing it as having substituted the rule of reason for a *per se* approach only with respect to "the general run of non-price vertical restraints." Appellant urges the Court to use this case as the vehicle for carving out an exception to *Sylvania* and establishing a new class of *per se* violations. (JS 19-21) In *Sylvania*, however, the Court emphasized that "we do make clear that departure from the rule-of-reason standard must be based upon demonstrable economic effect. . . ."[9] (433 U.S. at 58-59) On the record below there is no demonstrable economic effect which could justify any finding of antitrust wrongdoing, let alone a *per se* violation. There was and could be no weighing of "all of the circumstances . . . in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition." (*Id.* at 49) Of necessity, therefore, the Kansas franchise provisions must be examined on their face.[10]

9. *See, also, White Motor Co.* v. *United States*, 372 U.S. 253, 263 (1963) ("We need to know more than we do about the actual impact of these arrangements on competition to decide whether they have such a 'pernicious effect on competition and lack . . . any redeeming virtues' ").

10. As the Court has stated:

> "Although it is possible that specific future applications of [the statute] may engender concrete problems of constitutional dimension, it will be time enough to consider any such problems when they arise. We deal here only with the statute on its face." *California* v. *LaRue*, 409 U.S. 109, 119 n.5 (1972), *quoting Joseph E. Seagram & Sons, Inc.* v. *Hostetter*, 384 U.S. 35, 52 (1966).

2. *H.B. 2020 is designed to stimulate interbrand competition.*

On their face, the provisions of H.B. 2020 are wholly consistent with the stimulation of interbrand competition, including price competition, among the literally hundreds of competing brands of a far larger number of suppliers which have been available in other states (by comparison with just the 260 brands of only 80 suppliers identified in trial exhibits as available in Kansas under the former "open wholesaling" system). (18a) Particularly is that true in light of the prior absence of meaningful interbrand competition in Kansas which was revealed in the report of the legislature's Special Committee. It is clear from the legislative background of H.B. 2020 that its franchise provisions, far from representing a sinister candidate for *per se* antitrust treatment, were intended to promote price and service competition previously lacking in the Kansas liquor trade.

Clearly no federal law requires that all who wish to purchase a particular product must be permitted to do so. No federal law requires that all liquor wholesalers must have access to the purchase of all brands.[11] In fact, where suppliers' products reach ultimate consumers through middlemen, this Court has declared that "the right to select . . . customers may well be the most essential factor in the maintenance of . . . service" or other competitive criteria. *United States* v. *Bausch & Lomb Optical Co.*, 321 U.S. 707, 728-29 (1944).

11. *United States* v. *Colgate & Co.*, 250 U.S. 300, 307 (1919) ("[The Sherman Act] does not restrict the long recognized right of a trader or manufacturer, engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal"); *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365, 376 (1967) (". . . A manufacturer of a product, other and equivalent brands of which are readily available in the market, may select his customers, and for this purpose he may franchise certain dealers to whom alone he will sell his goods. . .").

In addition, in *Sylvania* the Court recognized that vertical restrictions going beyond a refusal to deal other than just with those franchised by the supplier, notwithstanding their elimination of intrabrand competition at the level of the middlemen, can enhance competition overall by achieving efficiencies and heightening the thrust of the supplier's products in interbrand competition with those of competing suppliers. The Court concluded that interbrand competition is the "primary concern of the antitrust laws" and the ultimate protection of consumers, because without it no amount of intrabrand competition can insure the availability of substitute competing products and the "significant check on the exploitation of intrabrand market power" thus provided by the existence of interbrand competition. (433 U.S. at 52 n.19)

Sylvania establishes that selective designation of wholesalers and vertical restrictions upon where and to whom they can resell, designed to maximize sales based upon the rendition of services furnished by wholesalers committed to building volume for a particular supplier's product, can be wholly consistent with the objectives of the antitrust laws. Such arrangements prevent other "free riding" wholesalers, who elect not to undertake and bear the cost of promotional, volume-building efforts, from reaping the benefits of such interbrand competitive activities performed by designated distributors obligated to maximize sales for the supplier. By reducing the volume they sell, "free riding" discourages the designated wholesalers from providing such competitive services because the costs incurred cannot be recovered.

H.B. 2020 advances the legitimate legislative purpose of orderly, efficient and competitive marketing designed to facilitate ready availability of many competing brands at all types and sizes of retail outlet in sufficient locations to insure convenient access to consumers and to encourage price competition and the provision of a variety of pro-

competitive wholesaler services. It does this by means of supplier selection of wholesalers obligated to invest their time, effort and money in furnishing all of the services necessary to promote sales of that supplier's particular brand in the most effective competition with those of other suppliers, enhancing brand recognition and consumer demand for and satisfaction with that brand.

As the trial evidence indicated, because of the importance of brand recognition in the minds of consumers, the industry deems it essential that brands be available in every outlet where they can be placed, that desirable shelf or display space be obtained at retail establishments everywhere possible, that the wholesalers educate the retailers about the brands they carry and persuade them to recommend them to consumers, that full stocks in all sizes be continually and readily available for prompt delivery to retailers wherever located, and that wholesalers provide a variety of other services, all of which are designed to build the brand and increase consumer call for it. The provision of these services is necessary not merely to realize the enhanced sales volume which results from a wholesaler's engaging in total account coverage, but also because even the few brands most heavily advertised by the suppliers cannot achieve their potential without promotional support, furnished in each local market by the wholesalers, which wins retailer and consumer acceptance of the brand and thrust for its advancement. Wholesalers protected from the "free rider" problem become willing to undertake the commitment and cost of furnishing their panoply of volume-building services not only for leading brands but also for newly introduced, less successful or even struggling brands.

Consistent with securing the broadest possible account coverage in order to achieve both maximum volume and enhance consumer awareness and demand for the brand, a wholesaler must be willing and H.B. 2020 obligates him

to serve on a non-discriminatory basis the large number of small, distant and marginal outlets which are costly to serve; he cannot concentrate solely on the large retail stores, which offer him greater profit potential but which, alone, are unable to provide the total volume for the brand which flows from marketwide availability and visibility when it is placed and featured in every possible outlet.

The existence of many retail accounts which are at best marginally profitable because of the higher costs of serving them, coupled with the lowering of the average unit costs of distributing a brand when duplication of services is avoided by placing it with one wholesaler (with resulting economies of scale), supports the adoption of the exclusive distribution established by H.B. 2020 as the lowest cost, most efficient means to introduce new brands and keep existing brands in fully effective, vigorous competition with those of other suppliers.

Appellant, however, conjectures here that a variety of anticompetitive consequences will accompany the enactment of H.B. 2020. Urging that "prices to consumers will increase to reflect the monopoly status of the surviving wholesalers," appellant cites opinion testimony by an academician that "open wholesaling" and intrabrand competition allegedly "led to lower prices" (appellant later recognizes that such competition could keep prices down only to "the lowest level permitted by law"). (JS 11, 13) Not only does the legislative history demonstrate that the high state-mandated markups sheltered costly, economically unjustifiable practices at the wholesaler level and held a guaranteed profit-protecting umbrella over even the most inefficient, but the sole record evidence[12] is that with the

12. The newspaper report cited by appellant (JS 17 n.8) is not of record. If, as appellant argues without record support, retail prices have risen since H.B. 2020, such increases could reflect increases in supplier prices to wholesalers or retailers taking higher markups even though interbrand competition could have forced wholesaler markups below the prior mandatory percentages.

advent of H.B. 2020 at least Standard, the wholesaler then accounting for the largest volume on a statewide basis, posted lower prices than the pre-existing minimum markups.

Similarly, appellant ignores the fact that suppliers in their own self-interest will seek those efficient wholesalers who, while rendering full services to all accounts, will maintain low, competitive markups. Once a supplier sets his affirmation FOB price to his wholesaler, the supplier can derive no benefit from the wholesaler's markup since any increase in price at that level goes into the wholesaler's pocket, not the supplier's. Once his price is set, the supplier's only interest is in maximizing his own profits by maximizing the volume of sales of his brands. That goal is best achieved by the lowest wholesaler markup. As this Court recognized in *Sylvania,* a supplier will select the middleman who provides the distribution and service which most effectively market his products at the lowest cost. As the Court stated:

> " 'Generally a manufacturer would prefer the lowest retail price possible, once its price to the dealers has been set, because a lower retail price means increased sales and higher manufacturer revenues.' [Citation omitted] In this context, a manufacturer is likely to view the difference between the price at which it sells to its retailers and their price to the consumer as its 'cost of distribution,' which it would prefer to minimize." (433 U.S. at 56 n.24)

The economic logic of this analysis is equally applicable to wholesaler prices to retailers.

Appellant also speculates that there is no limit to the number of suppliers and brands that "one distributor may tie up in the state" and that "interbrand competition may be reduced to a 'shadow-boxing' exercise within the sales

force of a single distributor." (JS 5) Again appellant chooses to ignore the economic self-interest of suppliers who, by any stretch of the imagination, cannot be assumed willing to countenance anything less than full "heavyweight championship" representation of any brand exclusively franchised to a wholesaler. In fact, the evidence below demonstrates that in the negotiation of franchises suppliers carefully explored what competing brands a particular wholesaler would be handling and refused to place any brand with him that was in direct, head-to-head conflict with some other supplier's brand for which he was franchised.[13] Moreover, appellant implies that the franchise agreements required by H.B. 2020, once filed, are "in perpetuity." (*e.g.*, JS 20) Apart from the fact that such agreements are made expressly subject to termination or alteration during their term for reasonable cause (47a-48a), §14-4-26(a)(7) of the Kansas Rules and Regulations Relating to Alcoholic Liquor provides that franchises may be limited to a definite period.

In support of its contention that at the wholesaler level "severe oligopolistic conditions [have been] brought about by H.B. 2020," appellant relies at length upon supposed "market share" data.[14] (JS 8-10, 15-16) Those data are

13. Appellant's own exhibits show, for example, that such substantial direct competitors and leading brands as Seagram's V.O. and Hiram Walker's Canadian Club, Somerset's Tanqueray and Kobrand's Beefeater, General Wine's Chivas Regal and Somerset's Johnny Walker Black, Paddington's J&B Rare and Buckingham's Cutty Sark, Austin Nichol's Wild Turkey and Jack Daniel's Black Label, were franchised to different wholesalers in each market area.

14. Appellant also argues that at the supplier level of the industry there is allegedly a high degree of concentration and a small number of producers dealing in heavily advertised, strongly differentiated products. Appellant concludes that such an environment is scarcely "conducive to wide-open interbrand competition, or likely to be improved by the introduction of absolute intrabrand restraints." (JS 8, 16) Neither court below made findings to support that conclusion and, even accepting the erroneous "market share" data treated above,

(footnote continued on next page)

in fact simply statewide case sales by suppliers into Kansas for the year 1978, from which appellant has calculated, brand by brand, the totals which purportedly would have been sold by the newly franchised distributors had they had franchises for those brands in that period. As such, even apart from the fact that wholesaler sales to retailers do not necessarily occur in the same year shipments are received from the supplier, obviously appellant's figures do not reflect what is happening in 1980 under the new franchise system with heightened interbrand competition, the introduction of new brands and a host of other factors neither of record nor knowable at the time of trial.

Moreover, even for the year 1978 and on the assumptions made by appellant, those state-wide figures do not allow calculation of true market share percentages. The record demonstrates without contradiction that the entire state is not a single market. To the contrary, Kansas encompasses a number of separate, local geographic markets delimited by economic considerations, including the sharply higher costs of serving retailers the more distant they are from a wholesaler's warehouse. A wholesaler operating from a warehouse in eastern Kansas simply cannot compete for accounts in western Kansas. Consequently, only those wholesalers with warehouses in the same area, generally centered in one of the larger cities, are in effective competition with each other, and the relevant geographic market must be measured in terms of those competitive realities. *See, e.g., Standard Oil Co. of Cal.* v. *United States,* 337 U.S. 293, 299 n.5 (1949); *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 357, 359 (1963); *Tampa Electric Co.* v. *Nashville Coal Co.,* 365 U.S. 320, 327

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there is no persuasive evidence of record to sustain the sweeping claims of supplier oligopoly. In any event, if such oligopoly existed in Kansas it resulted from the "open wholesaling," minimum markup system and reflected neither the absence of supplier and brand concentration in other states where franchised distribution exists nor what will follow in Kansas from the introduction of interbrand competition.

(1961). In short, market shares must be calculated in each local area of effective competition, the only relevant markets for that purpose.

Obviously, as with Standard and the Famous Companies, when a wholesaler organization operates four or five warehouses across the state and competes in each of the several local markets, its proportion of total state sales will be higher than those for wholesalers, such as the appellant, who do not. Those statewide sales percentages offer no insight into true market shares measured by the actual relevant geographic markets. Indeed, they may conceal the fact that the wholesalers operating on less than a statewide basis may have higher shares of the one or two markets in which they compete. Such statewide figures unrelated to sales in each of the actual local market areas fail to support claims of oligopoly or dominance as to any market.[15]

Moreover, the types or generic categories selected by appellant for its share calculations (straights, blends, bonds, Canadians, scotch, gin and so on) are both too expansive and too narrow for relevant market definition and share-of-market purposes. They fail to reflect (1) the existence of distinct price categories within each of the overall type categories used solely for reporting purposes

15. Even on the erroneous statewide basis, appellant's selective references to the dominance allegedly resulting for some wholesalers with franchising are misleading. For example, appellant attributes to Standard shares of several generic types in excess of 60%. (JS 10) Apart from the deficiencies of that analysis touched upon above, the 1978 statewide volumes thus attributed to Standard constituted only minor proportions of the total spirits sold into Kansas that year:

	Attributed to Standard	*Approx. % of Total Spirits*
Rum	95%	5%
Tequila	88%	1%
Blends	65%	3%
Brandy	70%	1%
Cockails	69%	2%

and the minimal competition between brands of markedly different cost (a $15 bottle of Wild Turkey has insufficient cross-elasticity to be properly included in the same market with a $5 bottle of Ten High bourbon, but they are included in the same category for state reporting purposes) and (2) the fact that competition among brands has increasingly cut across the lines of generic types as substantial numbers of consumers have come to use vodka, rum, gin, blends, Canadians and even light bourbons interchangeably for the same mixed drinks.

Finally, appellant argues that H.B. 2020 "attempts to create an absolute bar to any consideration of the market effects of privately established agreements" and is "patently invalid on its face because it excludes consideration of the very economic and other factors that the rule of reason demands be taken into account." (JS 19) The answer to this contention is twofold.

First, appellant urges that H.B. 2020 should be overturned on its face even though, consonant with this Court's analysis in *Sylvania* of the pro-competitive benefits which may result from vertical restrictions upon distributors, the interbrand competition which is the objective of the statute may in fact create a significantly improved overall competitive environment in Kansas or arguably even a competitive utopia in which the optimum benefits conceivable for retailers and consumers might be achieved.

Second, H.B. 2020 creates an absolute bar to a full rule-of-reason evaluation of the competitive effects of any exclusive franchise agreements only if, contrary to appellant's apparent position, the statute is not a proper subject for application of the "state action" doctrine of *Parker* v. *Brown,* 317 U.S. 341 (1943), or of the Twenty-first Amendment. If either or both apply, then there is no basis for any valid claim of antitrust violation, but if neither does

then antitrust actions in federal court, with a full rule-of-reason evaluation, are available to private parties and the ~~agreements. (JS 6, 16)~~ government.

Appellee submits that H.B. 2020, as the Kansas Supreme Court concluded, does not contravene, purport to authorize or mandate any violation of the Sherman Act, and there is no substantial federal question concerning its validity under that Act. Appellant in effect asks this Court to read into the state legislation a conflict with federal law when none exists. In another case involving a challenge to state liquor regulations based upon alleged Sherman Act grounds, this Court declared:

> "In this as in other areas of coincident federal and state regulations, the 'teaching of this Court's decisions . . . enjoin[s] seeking out conflicts between state and federal regulation where none clearly exists.' *Huron Cement Co.* v. *Detroit,* 362 U.S. 440, 446. We find no such clear conflict in the present case. . . . [The state regulation] imposes no irresistible economic pressure on the appellants to violate the Sherman Act in order to comply with the requirements of [the state regulation]." *Joseph E. Seagram & Sons, Inc.* v. *Hostetter,* 384 U.S. 35, 45 (1966)

That same analysis applied to H.B. 2020 should end this appeal, and there is no need for the Court to deal with other considerations which would save the statute even if an antitrust conflict were shown.

B. The Franchise Provisions of H.B. 2020 Are Exempt from the Antitrust Laws Under the "State Action" Doctrine.

Even if the exclusive territorial franchise arrangements between private parties mandated by H.B. 2020 could be found to violate the Sherman Act on the record here, the

state's participation in that system qualifies it for exemption under the "state action" doctrine of *Parker* v. *Brown*, 317 U.S. 341 (1943). There can be no dispute but that the first requisite, reiterated in *Midcal*, is satisfied, *i.e.*, "the challenged restraint [is] 'one clearly articulated and affirmatively expressed as state policy' . . . ." (100 S. Ct. at 943) Appellant, however, claims that there is no state supervision of the restraints created by the state-mandated private agreements. (JS 6, 16)

As noted, H.B. 2020 obligates each franchised wholesaler, at the risk of mandatory license revocation, to serve all retail accounts in his designated territory and to do so on a non-discriminatory basis as to both price and services, which promote sales and build volume. Concededly, in the first instance the statute leaves to those most versed in the marketing of alcoholic beverages the negotiation of the franchises, their terms and obligations, their areas and their duration. Negotiation of all of these elements, however, is subject to the pro-competitive self-interest of the supplier in maximizing his sales volume through effective competition with the brands of other suppliers.[16] Moreover, even before a franchise has run its term, it may be terminated or altered by either party upon notice to the ABC, which must then notify all affected parties of the impending termination, modification or alteration. Thereafter, without limitation to just the two parties to the franchise, the statute provides that any aggrieved supplier or distributor is entitled to a court hearing as to whether the termination, modification or territorial alteration is for reasonable cause or violates the franchise agreement. (47a-48a)

16. The Special Committee of the legislature recommended that the ABC "be empowered to review and approve all franchise agreements and also may approve or prohibit any terminations or modifications of the franchise agreement which are not made for good cause." (E6) Regulations in support of this recommendation conceivably can be formulated once this litigation is finally resolved.

In *New Motor Vehicle Bd. of Cal.* v. *Orrin W. Fox Co.*, 439 U.S. 96 (1978), the Court found antitrust immunity for a state program involving no more supervision by the state in satisfaction of the second requisite for invoking *Parker* than is established by H.B. 2020. In *Fox,* the statute required an auto manufacturer, before entering into a new franchise within the market area of an existing franchisee, to obtain state approval upon a finding of good cause (including consideration of whether the existing franchisees were providing adequate competition and convenient service for the public) following an administrative hearing if the existing franchisee protested the establishment of the new dealership. Rejecting claims of privately initiated restraint of intrabrand competition in conflict with the Sherman Act, the Court held:

> "The dispositive answer is that the Automobile Franchise Act's regulatory scheme is a system of regulation, clearly articulated and affirmatively expressed, designed to displace unfettered business freedom in the matter of the establishment and relocation of automobile dealerships. The regulation is therefore outside the reach of the antitrust laws under the 'state action' exemption.
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> "... California has not [attempted to authorize and immunize private conduct violative of the antitrust laws]. Protesting dealers who invoke in good faith their statutory right to governmental action in the form of a Board determination that there is good cause for not permitting a proposed dealership do not violate the Sherman Act, ..." (439 U.S. 109-110)

As the Court characterized *Fox* in *Midcal,* "In view of the State's active role, ... the program was not subject to the Sherman Act." (100 S. Ct. at 943).

C. The Kansas Franchise System Is a Valid Exercise of State Control Over Its Liquor Distribution System Under the Twenty-first Amendment.

The Kansas Supreme Court found H.B. 2020 to be a constitutionally permissible state regulation of alcoholic beverages under the Twenty-first Amendment. Appellant mistakenly argues that the court held that the Amendment gave the state absolute, unfettered control over liquor, wholly unrestricted by the Commerce Clause or by federal antitrust law and contrary to this Court's ruling in *Midcal.* (JS 14, 17) Not only is the Kansas court's opinion replete with statements which disprove appellant's contention,[17] but that court would hardly have bothered to decide that H.B. 2020 does not conflict with the antitrust laws if it believed that the Twenty-first Amendment completely displaces the Sherman Act where liquor is concerned.

In *Midcal,* this Court, reiterated that "the Twenty-first Amendment grants the States virtually complete control over whether to permit importation or sale of liquor *and how to structure the liquor distribution system.*"[18] (100 S. Ct. at 946) (Emphasis added) That statement is wholly consistent with the broad sweep accorded to the Twenty-first Amendment from its adoption, including the charac-

17. The state court, *inter alia,* said that liquor "has traditionally been a subject of governmental regulation at both federal and state levels" (14a); "the Twenty-first Amendment grants broad regulatory powers to a state with regard to intrastate regulation of liquor traffic . . ." (15a); ". . . the Twenty-first Amendment did not repeal the Commerce Clause . . ." (16a); and ". . . the weight of authority, both federal and state, . . . supports the broad regulatory power of a state in the area of alcoholic liquor . . ." (18a). The Twenty-first Amendment statements of the state court are wholly consistent with this Court's analysis in *Midcal.*

18. Appellant's suggestion (JS 22) that only state-owned or monopoly distribution systems are covered by the emphasized language is totally unsupported. Neither *Midcal* nor any other decision lends any support to that contention.

terization by Justice Brandeis in *State Board* v. *Young's Market Co.*, 299 U.S. 59, 63 (1936), "Can it be doubted that a State might . . . channelize desired importations by confining them to a single consignee?" While the court below correctly recognized that the federal government retains some Commerce Clause authority over liquor, structuring their liquor distribution systems has always been and continues to be a matter of "virtually complete control" by the states under the special authority granted to them by the Twenty-first Amendment. *Midcal* teaches that where competing state and federal interests are shown to exist they must be balanced and reconciled only after careful scrutiny in a "concrete case." (100 S. Ct. at 946)

In *Midcal,* the clear federal interest in price competition and the *per se* outlawing of private vertical price-fixing were confronted only by California's claimed interest in temperance and the preservation of small retailers against their larger competitors. Even in that context, however, this Court did not make an independent judgment that the asserted state interests were less substantial than the clearly defined federal policy against price-fixing. Instead, the Court looked to the findings of the California administrative agency and courts that private price-fixing did not in fact advance the asserted state interests. This Court then concluded that nothing in the record suggested the contrary. Therefore, while noting that state court findings are not binding on this Court to the extent that they undercut states rights guaranteed by the Twenty-first Amendment, consonant with established principles of deference to state court construction of state law and findings of fact, this Court concluded that it had "no basis for disagreeing with the view of the California courts that the asserted state interests are less substantial than the national policy in favor of competition." (100 S. Ct. at 946-948) Making clear that on a different record an opposite result could follow, the Court stated:

> ". . . We need not consider whether the legitimate state interests in temperance and the protection of

> small retailers ever could prevail against the undoubted federal interest in a competitive economy. The unsubstantiated state concerns put forward in this case simply are not of the same stature as the goals of the Sherman Act." (100 S. Ct. at 948)

On the record here, there is similarly no basis for this Court to disagree with the statutory construction and findings of the Kansas Supreme Court which support, rather than undercut, the state rights guaranteed by the Twenty-first Amendment. As distinguished from the California courts' rejection in *Midcal* of unsupervised vertical price-fixing by private parties on factual findings that the otherwise legitimate state interests asserted there were not advanced by higher consumer prices, here the Kansas Supreme Court has found that there is no evidence that the statutory changes effected by H.B. 2020 are not achieving their legislative purpose. That those purposes are not legitimate state police power policy objectives, even apart from the special powers over liquor granted by the Twenty-first Amendment, cannot be seriously argued. Introducing price competition at the wholesale tier as a means of lowering consumer prices, not only to achieve that salutary public interest but also to curb illegal out-of-state purchases at prices lower than those in Kansas under the pre-existing mandated minimum markups, thereby saving the state from the loss of substantial tax revenues, would be wholly valid state purposes even if a commodity other than liquor were involved. (20a-23a)

On their face, the provisions of H.B. 2020 not only fail to mandate or authorize violations of the federal antitrust laws but there is no basis for concluding that they are not reasonably related to achieving the legislative purposes. Because exclusive franchises and vertical restrictions can enhance interbrand competition by achieving scale economies and distributional efficiencies, they must be shown upon a full rule-of-reason analysis to cause an unreasonable

restraint of trade before any conclusion can be drawn that they are contrary to federal antitrust policy and interests in competition. The achievement of lower costs and vigorous interbrand competition through such restrictions, fueled by the interacting self-interests of both suppliers and franchised wholesalers in maximizing sales of their brands, are the wholly reasonable means adopted in H.B. 2020 for achieving the legislative purposes.

On this record, appellee submits that there are in fact no competing state and federal interests which require reconciliation, and H.B. 2020 is an unquestionably valid exercise of state rights under the Twenty-first Amendment.

Conclusion

For all of the reasons set forth above, appellee urges that the appeal be dismissed or, in the alternative, that the judgment of the Kansas Supreme Court be affirmed for want of a substantial federal question.

Respectfully submitted,

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APPENDIX

Report of Special Committee on Kansas Liquor Laws

To: Legislative Coordinating Council

From: Special Committee on Kansas Liquor Laws

Re: Proposal No. 16—Liquor Laws*

Under Proposal No. 16, the Special Committee on Liquor Laws was directed to conduct "a study of the laws of Kansas relating to the sale, distribution, price control, and state regulation of liquor and other alcoholic beverages."

Background

On November 2, 1948, the people of Kansas adopted an amendment to Section 10, Article 15, of the Kansas Constitution which authorized the Legislature to regulate, license, and tax the manufacture and sale of intoxicating liquors. The 1948 amendment also declared that "the open saloon shall be and is hereby forever prohibited." As a result of this amendment, the 1949 Legislature enacted the "Kansas Liquor Control Act" (K.S.A. 41-101 *et seq.*) which provides for the regulation of all phases of the manufacture, distribution, sale, possession, and consumption of alcoholic liquor. The Act is administered by the Division of Alcoholic Beverage Control of the Department of Revenue. Except for the 1965 and 1978 amendments and some relatively minor modifications which have been approved, the Liquor Control Act has remained virtually unchanged since 1949. The one major amendment to the 1949 Act took place in 1965, when the "Private Club Act" (K.S.A. 41-2601 *et seq.*) was enacted to close a loophole in the statute

* S.B. 28, S.B. 29, S.B. 30, S.B. 31, H.B. 2018, H.B. 2019, H.B. 2020 and H.B. 2021 accompany this report. Also accompanying this report are two Concurrent Resolutions recommended for introduction by the Committee.

under which numerous phony "private clubs" were established. The Private Club Act allows the consumption of liquor by the drink in licensed private clubs, which now total over 1,000 throughout the state.

The 1978 Legislature enacted another major modification to the Act through the passage of S.B. 975, the so-called "Restaurant-Club Act." This bill authorized the sale of liquor by the drink in certain bona fide restaurants. However, during the course of this study, the Kansas Supreme Court held S.B. 975 to be unconstitutional as violative of the "open saloon" prohibition of the Kansas Constitution. (*State ex rel. Schneider* v. *Kennedy,* 225 Kan. ——).

Committee Activity

In order to become familiar with the scope and operation of the Kansas liquor laws, the Committee received extensive briefings by the Director and other staff of the Division of Alcoholic Beverage Control (ABC). These briefings covered virtually all aspects of state regulation of the liquor industry and the functions and responsibilities of the ABC Division. Individuals from all segments of the liquor industry were also invited to present their views and concerns for Committee consideration. In addition to several manufacturers, a number of distributors and an even larger number of retailers appeared before the Committee. Testimony was also received from private club and tavern owners, several trade associations representing various segments of the industry, federal liquor enforcement officials, two Minnesota State Legislators, an economist, and numerous interested persons, including the former Revisor of Statutes who drafted the Liquor Control Act. Committee

staff also prepared various memoranda relevant to the study.

While a large number of conferees asserted that the Kansas liquor laws were functioning adequately to fulfill their statutory purposes, numerous minor changes were recommended to "fine tune" and modernize the statutes. (A summary of these relatively minor changes which were recommended is available from the Kansas Legislative Research Department.) The Committee thus devoted much of its deliberations to three major policy questions:

1. Should the existing "open wholesaling" provision of the Liquor Control Act be replaced by an exclusive franchise system?
2. Should the State of Kansas continue to set the minimum prices at the wholesale and retail levels and establish minimum markups at both levels?
3. Should the people of Kansas be permitted to vote on the question of repealing the "open saloon" prohibition?

Open Wholesaling. The Liquor Control Act prohibits exclusive distributorship arrangements and requires manufacturers to sell a product to all wholesalers. Wholesalers are, in turn, required to sell the product to all retailers on an equal basis. Apparently only two other states, Oklahoma and, since 1975, Minnesota, utilize an open wholesaling system. Representatives of Kansas distributors argued that the open wholesaling system curtails the illegal activities which sometimes occur in franchise states, prevents out-of-state manufacturers from exercising undue influence over Kansas distributors, and enhances the "orderly market"

which is one stated purpose of the Act. Other testimony stated that the independence of the wholesaler would be strengthened under a franchise system and illegal activities could be minimized through the adoption of mechanisms to protect the wholesaler from arbitrary acts by the manufacturer. It was also stated that open wholesaling forces all distributors to carry nearly-identical inventories and compete only on the basis of increased service: it was argued that both of these practices result in higher costs and higher consumer prices.

Minimum Pricing. Under the Liquor Control Act, the minimum sales price for liquor at the wholesale and the retail level is established by the Alcoholic Beverage Control Board of Review on the basis of statutory guidelines, which include acquisition costs, taxes and license fees, selling costs, transportation costs, reasonable expenses, and a reasonable markup or profit. The present markups permitted to wholesalers and retailers are as follows:

Product	*Wholesaler*	*Retailer*
Spirits	15½%	28½%
Cordials	17½%	36½%
Wines	26½%	45½%

Proponents of continued price maintenance by the state asserted that the provisions eliminate illegal activities which could result from intense economic pressure, curb ruthless commercial behavior by large competitors, prevent organized crime from entering the Kansas market, and support an orderly market. Proponents also argued that the liquor industry is highly regulated, not unlike some utilities, and that state regulations of this product is appropriate. Other conferees opposed to minimum pricing

stated that it contributes to higher consumer costs, rewards economic inefficiencies, and is, in effect, a guaranteed profit for established wholesalers and retailers.

"Open Saloon" Prohibition. In 1970, the voters of Kansas rejected a proposed constitutional amendment to repeal the "open saloon" prohibition by a vote of 335,094 to 346,423. Proponents of conducting another referendum on this question stated that a rational liquor by the drink provision cannot be enacted until this prohibition is removed; that sufficient changes have occurred in the state to warrant the submission of the question to the voters, who have not had the opportunity to speak on the issue since 1970; and that the amount of interest generated by voting on the "Restaurant-Club Act" indicates that a majority of the state's voters are supportive of repealing the 1948 prohibition. Opponents of submitting the question in a referendum asserted that any relaxation of the liquor laws will lead to increased use and abuse of alcoholic beverages.

Conclusions and Recommendations

Upon the basis of this study, the Committee concludes that the bulk of the Kansas liquor laws are operating adequately and in conformity with the intent of the enactments and do not require modification at this time. However, the Committee has reached the following conclusions regarding specific areas of the liquor laws:

1. *Open Wholesaling.* The open wholesaling system should be replaced with an exclusive franchise system which grants territorial protections to wholesalers and protections aganist arbitrary and illegal acts to both wholesalers and retailers. The franchise system proposed is intended to

eliminate many of the economic inefficiencies fostered under the present system; to introduce a measure of free enterprise and competition into the wholesale liquor industry while, at the same time, providing a level of continuity which will sustain an orderly market; and to result in more equitable prices for consumers while permitting reasonable profits to wholesalers and retailers. Conversion to an exclusive franchise system, with territorial and other protections, will eliminate the need for all Kansas wholesalers to carry nearly identical inventories and thus eliminate the economic inefficiency of duplicative inventories. Under the proposed franchise system, wholesalers are protected from arbitrary and illegal activities by manufacturers and retailers are protected against similar acts by wholesalers. In addition, the state will no longer establish minimum prices at the wholesale level: this will be an item for negotiation in the franchise agreements. Enforcement activities will not be hindered by the change since the Director of Alcoholic Beverage Control will be empowered to review and approve all franchise agreements and also may approve or prohibit any terminations or modifications of the franchise agreement which are not made for good cause. The Committee believes that establishment of an exclusive franchise system will bring about a more efficient and economical liquor distribution system and will also contribute to an orderly market in which consumer prices will be maintained at equitable levels. Hopefully, the prices on a number of products will be reduced under the proposed franchise system. The Committee was presented an estimate by the Division of Alcoholic Beverage Control that during 1977 Kansans illegally purchased $17 million worth of liquor from out-of-state sources, resulting in an enforce-

ment tax loss to the state of $680,000 and a gallonage tax loss of $1.5 million. If the franchise system does result in lower prices, the tax loss to the state should be reduced as fewer people will purchase out-of-state liquor illegally. The Committee recommends that Senate Bill 28, which will effect this recommendation, be enacted.

2. *Minimum Retail Prices.* The Committee recommends that the state continue to grant minimum price markups to licensed retailers. While elimination of price controls at the retail level would certainly enhance competition, the economic effects could be extremely detrimental to the present retail industry. Estimates were received that, should price controls be removed, as may as 80 percent of the present 1,200 retailers may be put out of business. While the Committee believes that there are too many retail stores in the state and that the price control system furthers economic inefficiencies, the Committee does not recommend that an upheaval on the retail level of this magnitude be created through the premature elimination of price controls. The Comimttee is recommending that a new registration fee be established as one means of limiting the number of retail outlets. The Committee believes that reduction in the number of retail liquor stores should be a topic of continued legislative interest in the future since the degree of economic efficiency at that level will remain low unless and until many of the inefficient stores are eliminated. The Legislature should also monitor the feasibility of removing retail price controls at some future time.

3. *"Open Saloon" Prohibition.* The Committee feels strongly that the time has arrived to again submit to the people of Kansas a proposed constitutional amendment to

repeal the "open saloon" prohibition. Repeal of this obsolete provision, which was very narrowly defeated in 1970, is a matter of broad statewide importance upon which the people have a right to speak, including the substantial number of young persons who have attained voting age since 1970.

In the opinion of the Committee, the "Private Club Act" is a law supported by an array of legal fictions and ingenious definitions, representative of a circumlocutious end-run around Article 15, Section 10, of the Constitution. With over 1,000 "private clubs" serving liquor by the drink across the State of Kansas, the hypocrisy, disdain, and ridicule engendered by this Act is quite understandable. The Committee received an estimate from the Department of Revenue that, of the approximately $142 million in liquor sales reported during calendar year 1977, between $19.5 million and $20.5 million worth of liquor was ultimately consumed in a private club. This estimate indicates that 13.7 percent to 14.4 percent of the liquor being consumed in Kansas passes through private clubs. With the liquor pool, the hotel exemption, the coupon books, the membership fee and waiting period, the Class A club or Class B club distinction, it is little wonder that tourist and Kansan alike are confused by the multiplicity of such requirements. Especially unfortunate is the fact that the term "open saloon" apparently encompasses jetliners traversing the skies of Kansas: countless air travelers will remember Kansas only as the place where no liquor could be served while the airplane was over the state. The Private Club Act invites abuse, begets hypocrisy and creates widescale enforcement problems.

During the course of this study voters in 45 Kansas counties, which contain nearly 75 percent of the state's

population, were permitted to vote on the "Restaurant-Club Act." Of the total votes cast, nearly 60 percent were in favor of permitting the consumption of liquor by the drink in bona fide restaurants. Although the adverse decision by the Supreme Court rendered these votes void, the number of Kansans supportive of liquor by the drink indicates that a referendum on the issue is desirable at this time.

The Committee recommends two resolutions for consideration by the 1979 Legislature: one would repeal the "open saloon" prohibition, while the other would repeal the prohibition but permit the sale of liquor by the drink only on a county option basis. The Committee has no preference between the two resolutions. However, the Committee strongly recommends that the voters of Kansas be permitted to speak on this important issue. If the proposed amendment is approved, the Legislature can then develop a rational, workable, enforceable liquor law which will be free of the infirmities and defects of the existing statute.

4. *Registration Fee.* The Committee recommends that a new registration fee of $1,000 be established for retail license applicants. As noted above, the Committee believes that there are too many (1,200 plus) liquor stores in the state. This fee is intended to discourage new liquor store license applications. Hopefully, it will serve to reduce the number of stores and thus permit greater economic efficiencies to be achieved by the remaining fewer stores. Senate Bill 29 will establish this new fee.

5. *Election Day Closings.* The Committee recommends repeal of the provision which requires retail stores, taverns,

and cereal malt beverage (3.2 beer) retailers to close on election days during the hours the polls are open. While there may have been some valid reason for this provision during the frontier days of Kansas, no case can be made to continue this obsolete provision in contemporary society. It is ironic that there is no requirement that private clubs close on election days. House Bill 2021 will effect this recommendation.

6. *Violations by Retailers.* The Committee recommends that the Director of Alcoholic Beverage Control be given the authority to levy monetary fines, up to $1,000, on retailers for violations. At present, the Director is only authorized to suspend or revoke the retailer's license. This new provision would permit the Director to use more discretion in making the punishment fit the violation. Additionally, another recommended bill will create a rebuttable presumption that, in violations involving sales to minors, the retailer knew or should have known that the person was a minor. This provision should ease the burden on some retailers who are fooled by fraudulent identification cards in the possession of mature-looking minors. Senate Bill 30 and Senate Bill 31 will effect this recommendation.

7. *Location of Retail Stores.* The Committee recommends House Bill 2019, which would permit retail liquor stores to be located in enclosed shopping malls. At present, retail stores cannot be located in such malls because K.S.A. 41-711 requires that stores not open into another business. The bill would permit stores to open into the common area of an enclosed mall but would not permit stores to have inside entrances into other businesses. Given the number of enclosed shopping malls in the state, this appears to be

an appropriate amendment at this time. House Bill 2019 would carry out this recommendation.

8. *"Sunrise-Sunset Prohibition."* The Committee recommends that the "sunrise-sunset" provision be repealed. Under this provision, wholesalers may not move alcoholic liquors from their warehouses before sunrise or after sunset. This appears to place a burden on some wholesalers, especially in the western part of the state, who must cover large delivery territories. One result of the proposed franchise bill may be to reduce the number of wholesale branch houses in the state which will result in even larger territories for some wholesalers. This change should also have no great effect on enforcement efforts. For these reasons, the Committee recommends enactment of House Bill 2020.

9. *Liquor Licensee Restriction.* The Committee recommends K.S.A. 1978 Supp. 41-311, which prohibits law enforcement officers and persons who appoint law enforcement officers from holding any liquor license, be amended. One effect of the present statute is to prevent liquor licensees from seeking election to some city offices. Evidently, the framers of this provision feared that a licensee who was also a law enforcement officer or who appointed law enforcement officers could influence the enforcement of the liquor laws to his or her own advantage. The Committee does not believe that this situation is a problem with respect to part-time law enforcement officers or city officials. The Committee recommends that the prohibition be limited only to full-time law enforcement officers. House Bill 2018 will make this modification.

10. *Payment of Gallonage Tax.* Several wholesalers expressed concern that the time schedule for payment of the liquor gallonage tax creates financial problems which result in increased expenses. Under the present law, the tax must be paid 30 days after the wholesaler receives the merchandise. Several wholesalers requested that the time period be increased by perhaps an additional 30 days. The Committee does not feel that it has the information necessary to forecast the impact of such a change, since relatively large tax revenues are involved. The Committee does recommend that the appropriate standing committees consider this problem to determine whether a less burdensome schedule could be developed without creating problem areas for the Department of Revenue.

Dec. 15, 1978

Respectfully submitted,

/s/ Frank D. Gaines
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Special Committee on Kansas
Liquor Laws

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Supreme Court, U. S.
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OCTOBER TERM, 1980

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v.

MICHAEL C. LENNEN,
SECRETARY OF REVENUE FOR THE STATE OF KANSAS, et al.,
Appellees.

On Appeal From the Supreme Court of the State of Kansas

Brief Opposing Motion to Dismiss or Affirm

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Kansas Division of Alcoholic Beverage Control—Report Concerning Shipments of Alcoholic Liquors by Classification and Brands from Distillers to Kansas Distributors for Fiscal Year July 1979 through June 1980 8

This brief replies to the motions to dismiss or affirm filed by the State of Kansas and by the intervenor/appellee Standard Liquor Corporation, the wholesaler made dominant by H.B. 2020.

I. On Its Face H.B. 2020 Defies Federal Antitrust Law.

At JS 18-20, appellant made the initial and central point that H.B. 2020 on its face patently contravenes federal antitrust law by commanding the formulation of unsupervised private territorial restraints, regardless of their effects. The State ignores this point. Standard unsuccessfully attempts to sidestep it. Standard Motion 18-19.

Standard suggests that H.B. 2020 has brought about "competitive utopia" (*id.*, 18)—hardly a surprising characterization from the viewpoint of the now dominant wholesaler whose market power is safeguarded by H.B. 2020, but an absolutely astonishing intimation from any other standpoint, especially given the record of the intensely anticompetitive effects of H.B. 2020 (*see* part IV, below). Standard's assertion not only departs from reality, it misses the point. Even under the rule of reason, the validity of airtight territorial restraints depends on a discriminating analysis of market context and circumstances and likely harms and benefits. H.B. 2020 precludes *all* analysis, of any variety, and substitutes *no* state supervision. It exonerates all ironclad territorial restraints, regardless of the circumstances. Consequently, on its face H.B. 2020 collides squarely with the Sherman Act under any test, and inquiry need proceed no further.

Standard's "second" set of contentions in this context appears at pp. 18-19 of its motion, where Standard cites the state action doctrine and the Twenty-first Amendment. The first half of this set of contentions may have been victimized by a scrivener's error. At p. 18, Standard's motion attributes to *appellant* reliance on the state action doctrine and the Twenty-first Amendment. Appellant's position is, obviously, precisely the opposite. In any event, neither the state action doctrine nor the Twenty-first Amendment provides Standard any solace against the facial invalidity

of H.B. 2020. The doctrine requires active state supervision, which is plainly absent, and, as *Midcal* establishes, the Amendment does not protect unsupervised private agreements that contravene the antitrust laws.

Standard also offers federal antitrust actions as a method for examining H.B. 2020's competitive effects (*id.*, 19), apparently as a cure for the statute's fatal facial deficiency. As noted in part IV below, the anticompetitive consequences of H.B. 2020 already have been amply demonstrated in the trial in state court in this matter. Further demonstration would be pointless (assuming any was ever needed, in light of the statute's facial invalidity), and nothing requires that such a showing must take place in federal, as opposed to state, trial court. Moreover, the complete answer to this intriguing suggestion by Standard is that states are not free to enact laws that literally defy the Sherman Act by relying on the subsequent availability of federal antitrust actions to attempt to rewrite the statute or deal with its anticompetitive consequences.

II. The State Action Doctrine Cannot Save H.B. 2020.

H.B. 2020 sets up *no* state supervision or control of the exclusive territories created by private parties; accordingly, the state action doctrine cannot save the statute. H.B. 2020 requires private restraints; the sole role of state liquor officials with regard to such restraints is to file the resultant contracts. Nonetheless, both the State and Standard assert the doctrine, the State by reference (without citation) to regulations "regarding the allocation and designation of territory" (State Motion 17) and Standard by reference to the potential for such regulations. Standard Motion 20, n. 16. Both contentions are wholly specious.

The State's principal witness, State Senator Frank Gaines (offered as an "expert" on the legislative intent behind the legis-

lation at issue) conceded at trial that H.B. 2020 provides no guidelines or safeguards for state supervision. R.T. (I) 98-99, 102. The text of H.B. 2020 (JS App. E) corroborates Gaines' concession. The only extant regulations on the point (which were promulgated *after* the trial of this matter) similarly set up *no* state supervision of the anticompetitive restraints at issue. Kans. ABC Regs. § 14-4-26, 4 CCH Liquor Control L. Rep. ¶ 6099V. Thus, the State's contention is baseless.[1]

Standard cites to a sentence from a Kansas legislative report (which it appends to its motion) "recommending" that the state ABC be empowered to review and approve all franchises. From this, Standard sees the potential for state regulations "once this litigation is finally resolved." Standard Motion 20, n. 16, and E6. This litigation has in no way impeded the promulgation of regulations, as shown by the *subsequent* promulgation of the regulations cited above. Moreover, the sentence cited by Standard is not a "recommendation" at all, and for Standard to espouse it is at least highly misleading. As is apparent from its actual text, the sentence is a description of the state franchise bill as phrased at the time the report was written. The report was prepared principally in support of state Senate Bill 28, the original Kansas franchise bill. In accord with the report statement cited by Standard, S.B. 28 contained language giving the state ABC supervisory power over franchise territories. *See* Def. Tr. Ex. 3, at 242-B, *et seq.* However, as Senator Gaines testified at trial, S.B. 28 died in committee. R.T.(I) 77-78. Components of S.B. 28 were then transferred to H.B. 2020, which started out as simply a repeal of a "sunrise-sunset" prohibition (Standard Motion E11), but which became the franchise bill actually enacted. R.T.(I) 77-78. In substituting an expanded H.B. 2020 for the unsuccessful S.B. 28, the legislature *dropped* the ABC supervisory language

1. At p. 10 of its motion, the State refers to a network of state regulation of the liquor industry in Kansas in general and confuses that with state control of the exclusive territories mandated by H.B. 2020. The statute does not give the State authority to exercise such control. Consequently, there is no state action defense.

of S.B. 28. In short, the Kansas legislature declined to enact the grant of authority to the ABC described in the report statement erroneously relied on by Standard to support its state action argument.[2]

III. Midcal Invalidates H.B. 2020.

The State and Standard both rely on the *Midcal* Twenty-first Amendment dictum about a state's "virtually complete control over . . . how to structure the liquor distribution system." *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 110 (1980); State Motion 6; Standard Motion 22-23. The reliance is misplaced. Read literally, the concept of *state* control over how "to structure the liquor distribution system" does not encompass *private* territorial restraints. Moreover, as a matter of logic, the *Midcal* dictum does not exonerate a private market division scheme any more than it does the private price fixing scheme struck down in *Midcal*. Clearly, *Midcal* does not approve state authorization of liquor cartels. Yet if appellees' interpretation of the *Midcal* dictum were correct, nothing would prohibit a state from requiring distributors to agree among themselves which territories to cover. In any event, if there is uncertainty on these points, it demonstrates the presence, rather than the absence, of a substantial federal question.

To date, the Kansas Supreme Court has not published its views on the meaning of the *Midcal* dictum relied on by appellees. However, in denying rehearing after *Midcal* came down, the Kansas court apparently shared appellees' interpretation of the *Midcal* dictum as a cover for anticompetitive private conduct. By contrast, the California courts quite recently have rejected the

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2. Standard's citation of *New Motor Vehicle Bd. of California v. Orrin W. Fox Co.*, 439 U.S. 96 (1978) (Standard Motion 21) is as misguided as its treatment of the legislative report appended to its motion. For example, as Standard's own description of *Fox* notes, the statutory system in *Fox* required *prior* state approval upon a finding by state officials of good cause. Nothing like that exists in H.B. 2020. Moreover, the statute in *Fox*, also unlike H.B. 2020, did not mandate unsupervised private territorial restraints.

essence of appellees' position. *Norman Williams Co. v. Rice,* 166 Cal. Rptr. 563, *hearing denied,* Cal. Sup. Ct., Case No. 19089 (Sept. 24, 1980) (*Midcal* "distribution system" dictum covers only such basic structural matters as the creation of a licensing system for imports.)[3] The dissonance, if not square conflict, between the positions of the two state court systems on this important point illustrates the existence of a substantial federal question.

The State and Standard also contend that *Midcal* applies only to *per se* antitrust violations, and not to rule of reason cases. State Motion 8-9; Standard Motion 7-8. Neither the text nor logic of *Midcal* supports that view, but—again—any doubt on the issue presents a substantial federal question. Moreover, there is again a conflict between appellee's contention (and therefore their reading of the essence of the judgment below) and the recent ruling of the California court in *Norman Williams, supra.* Applying *Midcal,* the *Norman Williams* court struck down a state statute despite noting the absence of a recognized *per se* antitrust violation. 166 Cal. Rptr. at 569.

IV. The Record Amply Demonstrates the Anticompetitive Effects of H.B. 2020.

In a remarkable effort to disguise what was presented to the state courts, appellants assert that there has been no showing in the proceedings below and no holding by the state trial court as to the "actual competitive experience" or the "market effects" which followed the enactment of H.B. 2020. State Motion 3, 8-9, 19; Standard Motion 5, 9. The record belies this preposterous assertion.

In its opinion, the trial court declared that "(t)he effect of the exclusive franchise system authorizes private persons to engage in anti-competitive conduct and constitutes a violation of the

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3. As noted at JS 22, n. 12, the decision in *Norman Williams* is by the same California intermediate appellate court that was affirmed by this Court in *Midcal.* In the interim since the filing of the jurisdictional statement, the California Supreme Court has denied review in *Norman Williams,* thereby leaving the intermediate court as the highest state court to rule on the question.

Sherman Act." JS App. B 36a. The trial court's conclusion is supported by extensive evidence presented at the trial, which scrutinized the harmful effects of H.B. 2020 upon the wholesale liquor business in Kansas. Plaintiffs' trial counsel included Mr. Paup, a former F.T.C. staff attorney and an experienced antitrust lawyer. Plaintiffs made a well-documented showing of the immediate and severe anticompetitive effects of H.B. 2020. The jurisdictional statement repeats the evidence introduced by plaintiffs at trial, as a study of the record will indicate.

By way of illustration: To demonstrate the impact of H.B. 2020 at the wholesaler level, plaintiffs introduced into evidence the territorial agreements with suppliers entered into by Standard and Famous, the wholesalers who became dominant under H.B. 2020. These, together with plaintiff's exhibit 2, which showed the monopolistic or duopolistic wholesaler market shares created by H.B. 2020 in almost every category of spirits, and defendants' exhibit 1, official state case sale figures described by counsel for defendants as the "best evidence" of case sales to Kansas wholesalers (R.T. (I) at 16), clearly established that H.B. 2020 severely impaired competition at the wholesaler level. Indeed, plaintiffs' exhibit 2 established that under H.B. 2020 the market share of Standard and Famous together exceeded 70% in no less than nine categories of spirits.

Appellees quibble about the mechanics of how market share data were proven. Yet they have made no attempt, either at trial or subsequently, to deny that Standard's market share under H.B. 2020 is approximately 50% and that Famous has about 25% of the overall market. Pl. Tr. Exs. 2-5.

Plaintiffs also established the disastrous effect of H.B. 2020 upon those wholesalers not favored by this special interest legislation. Jack F. Grant, president of appellant, and Albert C. Becker, president of Kansas Distributors, Inc., each testified that they had lost approximately two-thirds of their business as a result of H.B. 2020 and would probably not be able to remain in business. R.T.

(I) 25-26; R.T. (II) 27-28. State Senator Frank Gaines revealed that during the legislative deliberations he was aware that one effect of H.B. 2020 would be the demise of several Kansas distributors. R.T. (I) 86.

The trial court also heard testimony at length from a highly qualified expert witness, Dr. William Terrell, as to the extensive damage done by H.B. 2020 to competition and pricing in the Kansas alcoholic beverage industry. R.T. (I) at 109, *et. seq.* Dr. Terrell's extensive work in this field was praised by the Kansas Supreme Court, which noted his special expertise. JS App. A 5a. Terrell has given testimony before the state legislature on liquor legislation; he is the economist identified in the legislative report appended to Standard's Motion. See p. E2.

Extensive evidence was also presented as to the harmful effects of H.B. 2020 on interbrand competition. The State's own official case sales data were introduced to establish the sales into Kansas of each brand in each spirits category. From these data, the market share of each manufacturer can readily be determined. These state data prove that a handful of suppliers have most of the business in the state. See JS, App. F. The brands of these dominant suppliers are, as the president of Standard conceded at trial, heavily advertised and strongly differentiated in the minds of consumers. R.T. (II) at 67-68. (Standard acknowledges this in its motion. See p. 12.) This witness further conceded that under H.B. 2020 many dominant brands within the same categories had been allocated to the same distributor. R.T. (II) 66. This evidence demonstrates that interbrand competition in the state is substantially impaired, and it was into such an environment that H.B. 2020 injected a total ban on intrabrand competition.

Appellees do not deny the existence of supplier oligopoly. As in the case of wholesaler obligopoly, they attack appellant's methodology, but do not dispute its conclusions. Moreover, at trial appellees failed to rebut plaintiffs' proof of the effects of H.B. 2020. This failure is understandable; H.B. 2020 is plainly

and simply an anticompetitive statute. That reality cannot be wiped away by bucolic conjecture about the benefits of restraints on intrabrand competition in quite different market environments.[4]

Standard complains that appellant's market share figures "do not reflect what is happening in 1980 . . . ." Standard Motion 16. Since the trial occurred in 1979, this is hardly surprising. The market share data presented were for 1979, since they were the latest official data available at the time of trial. To suggest that appellant should have presented 1980 data in a 1979 trial is absurd. However, since Standard raises the point and the State has chosen to rely on 1980 statistics outside the record, appellant is compelled to point out that the State's own official "Report Concerning Shipments of Alcoholic Liquors by Classifications and Brands from Distillers to Kansas Distributors" for fiscal 1980 demonstrates that, in one category after another, the supplier and wholesaler oligopolies which dominated the Kansas market in 1979 (see JS, App. F) still do so in 1980.

V. The State Appendices Are Outside the Record, Misleading and of No Probative Value.

The appendices to the State's motion are based upon data outside the record and which postdate trial, and are in any event of no probative value. For example, Appendix A purports to reflect a major increase in "line items" available in Kansas, since H.B. 2020 went into effect. This suggestion is grossly misleading. A "line item" is no more than a "container" or size of alcoholic beverage. State Motion App. A, p. 1. The State fails to advise the Court that the alcoholic beverage industry is currently converting to metric sizes. Thus, the recent proliferation of "line items" cited by the State demonstrates nothing more than the

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4. Standard's principal point in its motion is a rendition of *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977). Standard Motion 8-9, 11-14. That rendition fails to point out that the restraint in *Sylvania* was engaged in by a firm with a no more than five percent market share and was of a less stringent type than the total ban on intrabrand competition created by H.B. 2020.

availability of familiar, old brands in numerous new metric sizes, as well as the traditional sizes.[5] Furthermore, the State's own report of shipments into Kansas for the fiscal year ending June 30, 1980 shows that there have been no significant inroads into the dominant positions of the leading suppliers in the basic spirits categories and no significant new market entries under H.B. 2020.

Appendices B-1 and 2 were supplied to the State by the Kansas chapter of the national association of wholesalers whose general counsel drafted H.B. 2020. Appendix B-1 establishes that in 33 out of 54 instances selectively cited by the State, the price of liquor under H.B. 2020 is higher than it was before the statute went into effect. This speaks for itself.

Appendix B-2 is also of no probative value. It merely establishes that in approximately half the instances selected by the State, the benefits of the state law requiring that suppliers affirm that their prices to Kansas wholesalers are the lowest available anywhere in the United States are going into the pockets of the wholesalers and are thus not being passed on to retailers or to consumers.

VI. Conclusion.

Appellees attempt to argue the merits. They fail in that attempt, but they also miss the point. They do not demonstrate the absence of a substantial federal question. To the contrary, their contentions (particularly the State's Questions Presented section of its motion) establish quite the opposite.

Despite the undisputed trial court evidence set forth in the jurisdictional statement, appellees insist that there is no record

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5. There has also been a change in a previous Kansas requirement that a supplier attest that it could supply the Kansas market for 60 days before it could ship an item into the state. Def. Tr. Ex. 3, at 302-B. This requirement has been dropped, allowing suppliers of special items, such as elaborate special edition decanters, and small "boutique" wineries, to sell a handful of cases of their products in Kansas to meet the small demand for them. This cannot be considered significant new entry.

of the actual anticompetitive effects produced by H.B. 2020. These claims are erroneous, but more importantly, both Standard and the State ignore the fundamental deficiency of H.B. 2020—its attempt to displace antitrust analysis of territorial restraints with a blanket imprimatur for their imposition. This Court has made clear that the states may not free private parties from federal antitrust requirements simply by authorizing or commanding them to engage in conduct forbidden by federal law. *Midcal,* supra, 445 U.S., at 105-06. In H.B. 2020, Kansas has done exactly that. By attempting to declare vertical restraints lawful regardless of supplier and distributor market share, and without any state mechanism for evaluating whether the utopian benefits hypothesized by Standard *may* be present, Kansas has decided that its wine and spirits industry shall be exempt from the Sherman Act. This Court's rulings show that Kansas may not so act and, rather than affirmance or dismissal, summary reversal is therefore appropriate.

Respectfully Submitted,

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